

THE INCOME TAX REPORTS

A JOURNAL OF
THE LAW OF INCOME TAX AND EXCESS PROFITS TAX
WITH
REPORTS OF
INDIAN AND SELECT ENGLISH CASES.

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Income Tax Reports.

VOLUME XI—1943.

PART I.

The New Year.

We are now entering upon the eleventh year of the *Income Tax Reports* and when we look back over the period of ten years that has elapsed since the commencement of this journal—a period which will ever be remembered for its unique importance in the development of Indian Income-tax law—we feel a glow of happiness at the good work that has been done. Throughout this difficult period we have spared no pains to report accurately and promptly all the reportable decisions on Income-tax law. We have watched very closely the proceedings of the Legislatures and placed before our readers their true trend and effect. We have also been giving periodically a review of the progress of the law of income-tax with our notes and comments. Whenever we felt that the law was going astray we have boldly pointed it out and shown the correct path and there are numerous instances in which our criticisms have finally prevailed. We need hardly say that our greatest encouragement during all these years was the appreciation of our readers, for there is no reward which a real artist values so much as the sincere appreciation of men of taste and culture. We resume our work wishing all our readers a happy new year.

Repeal of the Income-tax (Amendment) Act of 1939.

We have been receiving numerous enquiries as to the effect of the recent repeal of the Income-tax (Amendment) Act of 1939 by the Repealing and Amending Act, XXV of 1942: (*vide* 1942, 10 I.T.R. Statutes, p. 9). We also felt some surprise that the Legislature should have thought it necessary or expedient to repeal this important Act so soon. No doubt the impression under which the Legislature has now repealed the Amendment Act is that, as the amendments made by it have been incorporated in the Act of 1922 and have become part and parcel of the Act of 1922, the Amendment Act may be taken away from the statute book. The course adopted by the Legislature is unusual and unnecessary and we fear that it may lead to unexpected complications.

Repealing and Amending Acts are now and then passed by the Legislature to remove from the statute book Acts that were of temporary duration and had become obsolete. Amendment Acts are also repealed when a consolidating Act in which the amendments have been incorporated is passed. But we rarely find Amendment Acts

which are to be in effect repealed before passing a consolidating Act. If the view of the Legislature is correct an Amending Act may be passed to-day and may be repealed the next day or even the next hour or minute, because the amendments take effect immediately on the passing of the Act and become part of the main Act.

We shall not be surprised if the real effect of the repeal of the Amendment Act of 1939 is contested before the Courts, but would advise the public to proceed on the basis that all the amendments effected by the Act of 1939 continue in force, in other words, as if the Amendment Act of 1939 has not been repealed at all.

Assessment of Bar Councils.

Though the judgment of the Madras High Court in the matter of the *Madras Bar Council* (reported in this issue) is based on consent of parties and as such cannot be assailed, it raises some important questions of law relating to the assessment of professional bodies and institutions such as Bar Councils, Medical Councils, Nursing Councils, Engineer's Societies, etc., and Commissioners of other Provinces may be interested to know the correct legal position. The question that arises with regard to such bodies is whether their income is exempt from income-tax under Section 4 (3) (i) of the Indian Income-tax Act which relates to income derived from property held under trust for religious or charitable purposes. In order that income may be exempt under Section 4 (3) (i) the property from which it is derived must be held under trust or other legal obligation wholly for charitable purposes or if the property is so held in part only for such purposes, the income must be applied or finally set apart for application to such purposes. So far as income derived by such institutions in the shape of examination and enrolment fees is concerned it is not derived from any property held under any trust and such income is liable to tax. The difficulty is with regard to income from investments, and other property vested in the Bar Council. We have to consider *first*, whether such property is held under trust or any legal obligation for any purpose, *secondly*, whether that purpose is a charitable one and *thirdly*, if the property is held in part only for a charitable purpose, whether the income is applied or finally set apart for application thereto.

(i) Whether the property of a Bar Council is held under any trust or legal obligation has to be decided from the Bar Councils Act, the Rules framed thereunder, or the Resolutions of the Council. If there is nothing in any of these which creates a trust or other legal obligation to apply the income from investments or other properties for any particular purpose there can be no trust or legal obligation.

(ii) It has been settled by a series of decisions in the United Kingdom that the purpose of regulating and advancing the interests of professional bodies or institutions is not a charitable purpose; and further, that if the main and dominant purpose is the advancement of the interest of a profession the mere fact that incidentally it affords relief to the indigent members of that profession or advances the education of the members of that profession would not make the purpose charitable. To borrow an expression well known in constitutional law we have to be guided by the 'pith and substance' of the matter. The mere fact that incidentally it advances education is immaterial. Taking for instance, a simple case, if I set apart the income from a particular property for the maintenance of my poor relations or the education of my grandsons, would this fact make the purpose charitable and exempt the income from tax? The dominant purpose is not relief of the poor or advancement of education but the advancement of my relations or grandsons, though incidentally it may relieve their poverty or advance their education. The mere fact that certain funds are set apart for education is not enough. We have to go further and ask, 'for whose education?' Unless the purpose is one of general public utility the mere fact that it advances education or relieves poverty, would not make the purpose charitable. The question then is, is benefit to a professional body, benefit to the general public. This question has been considered again and again by the English and Scotch Courts and the weight of authority is clearly in favour of the view that a professional body or association is not part of the general public and a purpose beneficial to such body is not necessarily a purpose of general public utility. For a review of these cases reference may be made to *A. N. Aiyar's Commentary on the Indian Income-tax Act, Second Edition*, pp. 272-275.

(iii) The provision in Section 4 (3) (i) that if property is held in part only for such purposes the income applied or finally set apart for application thereto is also exempt, does not, in our view, overrule this principle, but only means that if property is held in part for a dominant purpose which is charitable, income applied or finally set apart for that dominant charitable purpose is to be exempted. This provision does not contemplate, *e.g.*, the separation of the amount set apart for education of a particular person or body of persons when this is only an incidental purpose, the main purpose being the general advancement or well being of that particular person or body. Property may be held in trust wholly for a charitable purpose or in part only for a charitable purpose, but in either case the purpose for which it is held wholly or in part must be dominantly a charitable purpose.

In our view the Appellate Tribunal has taken a correct view of the law applicable to such cases and but for the fact that the Madras decision

is one based on consent, it may be difficult to support it. We think income derived by a Bar Council from investments will not be exempt even if it is applied in fact for advancing the education of members of the Bar or apprentices-at-law. It is also clear that a mere statement in Court that such income would hereafter be applied for the education of the members of the profession would not make any difference, for it is certainly not sufficient to create a trust or other legal obligation contemplated by Section 4 (3) (i).

PARTIAL PARTITION OF HINDU UNDIVIDED FAMILY.

SIR SUNDAR SINGH MAJITHIA'S CASE.

The High Courts of India had been holding the view from the year 1934 that it is not open to the members of a Hindu undivided family to enter into a partnership in respect of a portion of the joint family property which they have partitioned amongst themselves and we had been consistently criticising this view as unsound. Commenting on *Biradmal Lodha's Case* [1934] (2 I.T.R. 164) in which such a proposition was first enunciated we said: "Though on the facts of the case the question was rightly answered in the negative the question as put is not capable of a broad answer.....The real test (as to whether Section 25A applies) is whether there was an intention to alter the *status*. If the idea of the members was to separate and destroy their joint status the mere fact that some of the properties were left out either intentionally or by mistake to be divided later on would not render 25A inapplicable." When the Lahore High Court decided in *Sundar Singh Majithia's Case* [1938] (6 I.T.R. 336) that unless there is a partition of all the family property Section 25A cannot be applied and the divided members cannot form themselves into a firm we said *vide* [1938] (6 I.T.R. Notes & Comments p. 42): "We entirely fail to see any justification whatever for the Income-tax authorities to ignore the legal results of a partial partition which is permitted by the Hindu Law. Section 25A prescribes the procedure to be followed when there is a complete partition. But this does not mean that the Income-tax authorities are entitled to ignore the legal effect of a partition of a property owned by the family. The question that arises in such cases is similar to cases of alienation or gift made by the family—whether the income in question continues to be the income of the undivided family within Section 3 of the Act. Partial partition removes the property divided from the ownership of the undivided family and the *income of the property divided ceases under law to be the income of that family within Section 3*. The real owners of that income, namely, the firm alone can be assessed in respect of that income under Section 3. *It is*

only when the members of a family claim that a general partition has taken place and the undivided family itself has ceased to exist that any necessity arises to invoke Section 25A."

We reiterated this view in 1939 in the First Edition of our *Income-tax Act* (Vol. II, p. 499) and in the year 1942, in the Second Edition, p. 526.

It must be a matter of much gratification to us and to our readers that the view for which we had been contending so long unsuccessfully in India has been emphatically laid down by the Judicial Committee in the appeal in *Sir Sundar Singh Majithia's Case* [1942] (10 L.T.R. 457). Sir George Rankin delivering the opinion of the Board says as follows :

"The contention of the Commissioner is that for the purposes of the Income-tax Act members of an undivided family cannot enter into a partnership in respect of a portion of the joint property which they have partitioned among themselves. But in their Lordships' view Section 25A contains no warrant for any such prohibition. *It has no reference at all to any case in which the Hindu undivided family remains in existence at the time of assessment.* No difficulty whatever in the assessment of a Hindu undivided family is caused—or was ever thought to be caused—by the fact that in one year it has certain assets and certain income therefrom and that in the next year it is found to have parted with one asset and to be no longer in receipt of the same income. *The same assessee has a different income in each year that is all.* It matters nothing whether the particular asset no longer possessed by the Hindu undivided family has become the separate property of the member or belongs to a stranger. Section 25A is directed to the difficulty which arose when an undivided family had received income in the year of account but was no longer in existence as such at the time of assessment.....*The section has nothing to say about any Hindu undivided family which continues in existence never having been disrupted. Such a case is outside sub-section (3) because it is not within the section at all.* No sub-section is required to enable an undivided family which has never been broken up to be deemed to continue. But it need not have the same assets or the same income in each year and it can part with an item of its property to its individual members if it takes the proper steps."

It will be observed that the views and ideas expressed by the Privy Council agree exactly with what we had stated four years ago. This is another outstanding instance in which the Judicial Committee has proved its great usefulness as a Court of Appeal from Indian High Courts and set aside an erroneous practice which was being followed for a number of years in India.

NOTIFICATIONS.

Income-tax Rules, 1922, R. 22A (Forms of Appeal to Appellate Tribunal)—Amendments.*Notification No. 58 dated the 12th December 1942.*

In exercise of the powers conferred by sub-section (1) of Section 59 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendments shall be made in the Indian Income-tax Rules, 1922, the same having been previously published as required by sub-section (4) of the said section, namely :—

In form R (T) appended to rule 22A of the said Rules—

(a) Below the words and brackets

“THE (INCOME-TAX) APPELLATE TRIBUNAL, DELHI” the following shall be inserted, namely :—

“In the matter of the assessment of (the name of the assessee)”, and

(b) for paragraph 4, the following paragraph and Note shall be substituted, namely :—

“4. that in arriving at the finding of fact mentioned at No. in paragraph 3 above the Bench committed the following error of law, namely, (here state concisely the error of law) and but for this error of law the correct finding would have been (here state the finding which the Bench should have reached).

Note.—If any other finding of fact is attacked on the ground that the Bench in arriving at it committed an error of law, paragraph 4 in that case should be numbered paragraph 4 (1) and each error of law stated in a separate sub-paragraph in the same form, as far as possible, as paragraph 4 (1).”

Boards of Referees—Panel of Persons.*Notification No. 54 dated the 14th November, 1942.*

In exercise of the powers conferred by rule 2 of the Excess Profits Tax (Boards of Referees) Rules, 1940, the Central Government is pleased to direct that the following further amendments shall be made in the notification of the Government of India in the Finance Department (Central Revenues) No. 1-Excess Profits Tax, dated the 11th January 1941, namely :—

In the Schedule annexed to the said notification, under the heading “Non-officials”, after entry No. 27C, the following entries shall be inserted, namely :—

27D. Mr. L. B. Gillies, Messrs. Peirce Leslie & Co., Ltd., Calicut.

27E. Mr. W. Grant, M.L.A., Messrs. Aspinwall & Co. Ltd., Cochin.

27F. Mr. B. Richards, Messrs. W.H. Brady & Co., Ltd., Broadway, Madras.

27G. G. Sriram Babu Esquire, B.A., B.L., Honorary Secretary, Andhra Chamber of Commerce Ltd., 9, Armenian Street, G.T., Madras.

27H. Rao Bahadur B. S. Tripuranthaka Mudaliar, o/o Malabar Chamber of Commerce, Calicut.

Notification No. 55 dated the 21st November 1942.

In exercise of the powers conferred by Rule 2 of the Excess Profits Tax (Boards of Referees) Rules, 1940, the Central Government is pleased to direct that the following further amendments shall be made in its notification No. 1-Excess Profits Tax, dated the 11th January 1941, namely :—

In the Schedule appended to the said notification, under the heading "Judicial Officers" for entries Nos. 12 to 15, the following entries shall be substituted, namely :

12. Mr. C. C. O. Alipi, Additional District and Sessions Judge, Coimbatore.

13. Mir Amiruddin Sahib Bahadur, District and Sessions Judge, Trichinopoly.

14. P. Ramalingam, I.C.S., District and Sessions Judge, Salem.

15. Mr. A. S. Panchapakesa Ayyar, I.C.S., District and Sessions Judge, North Arcot, Vellore.

15A. M. E. E. Mack, I.C.S., District and Sessions Judge, Bellary.

15B. Mr. M. Shahabuddin, I.C.S., District and Sessions Judge, Chingleput.

15C. Mr. P.M. Srinivasa Ayyangar, District and Sessions Judge, Ramnad.

Notification No. 60 dated the 19th December 1942.

In exercise of the powers conferred by Rule 2 of the Excess Profits Tax (Boards of Referees) Rules, 1940, the Central Government is pleased to direct that the following further amendment shall be made in its notification No. 1-Excess Profits Tax, dated the 11th January, 1941, namely :—

In the Schedule appended to the said notification, under the heading "Judicial Officers" for entry No. 12, the following entry shall be substituted, namely :—

12. C. C. O. Alipi Sahib Bahadur, District and Sessions Judge, South Kanara, Mangalore.

**Notification Applying Certain Enactments to British
Baluchistan.**

Notification No. 200 F dated the 27th October 1942.

In pursuance of sub-section (2) of Section 95 of the Government of India Act, 1935, the Governor-General in his discretion is pleased to direct that the Repealing and Amending Act, 1942 (XXV of 1942), shall apply to British Baluchistan.

Notification No. 100 W dated the 3rd December 1942.

In pursuance of sub-section (2) of Section 95 of the Government of India Act, 1935, the Governor-General in his discretion is pleased to direct that the Income-tax and Excess Profits Tax (Emergency) Ordinance, 1942 (Ordinance No. LX of 1942), shall apply to British Baluchistan.

Income-tax Establishments.*Notification No. 56 dated the 21st November 1942.*

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that with effect from the 1st November 1942, the following further amendment shall be made in the Schedule appended to its notification No. 58 Income-tax, dated the 15th July 1939, namely :—

In the said Schedule under the sub-head "I.—Madras—" entry No. (13), against the Trichinopoly Range shall be omitted.

Notification No. 57 dated the 28th November 1942.

In pursuance of sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue empowers the Inspecting Assistant Commissioner, Delhi, and the Commissioner of Income-tax, Delhi, to perform all the functions of an Inspecting Assistant Commissioner, and Commissioner of Income-tax respectively in respect of such incomes or classes of incomes and of such persons or classes of persons in the Hissar, Rohtak, Ambala and Simla income-tax circles as are likely to be assessed to Excess Profits Tax under the Excess Profits Tax Act, 1940 (XV of 1940).

Notification No. 63 dated the 19th December 1942.

In exercise of the powers conferred by sub-section (3) of Section 5 of the Income-tax Act (XI of 1922), the Central Government is pleased to direct that the following amendment shall be made in the Finance Department (Central Revenues) notification No. 3 Income-tax Establishments, dated the 27th January, 1940, namely :

For the words and figures "in the Provinces of Bombay, Sind and British Baluchistan with effect from the 1st September, 1939" the words, figures and brackets "with effect from the 1st September, 1939 in the jurisdiction of the Commissioner of Income-tax (Central), Bombay" shall be substituted.

Notification No. 69 dated the 19th December 1942.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that with effect from the 1st January 1943, the following further amendment shall be made in the Schedule appended to its notification No. 58 Income-tax, dated the 15th July 1939, namely :—

In the said Schedule under the sub-head "VI.—Bihar and Orissa—" for the ranges and income-tax circles specified thereunder the following ranges and income-tax circles respectively shall be substituted, namely:—

- | | |
|------------------------------|--------------------------|
| " Patna— | (6) Puri Ganjam-Koraput. |
| (1) Patna. | (7) Dhanbad. |
| (2) Special Circle, Patna. | (8) Santhal Parganas. |
| (3) Shahabad-Palawan. | Muzaffarpur— |
| (4) Gaya. | (1) Saran. |
| Purulia— | (2) Muzaffarpur. |
| (1) Ranchi-Manbhum Sardar. | (3) Champaran. |
| (2) Salaries Circle, Ranchi. | (4) Purnea. |
| (3) Hazaribagh. | (5) Darbhanga. |
| (4) Singhbhum-Sambalpur. | (6) Bhagalpur. |
| (5) Cuttack-Balasore. | (7) Monghyr." |

Income Tax Reports.

VOLUME XI—PART V.

BUDGET FOR 1943-44.

NEW TAXATION PROPOSALS.

The Budget for 1943-44 introduced in the Central Assembly on February 27 by Sir Jeremy Raisman, Finance Member, disclosed a revenue deficit of Rs. 94.66 crores for the current year and a prospective deficit of Rs. 60.29 crores next year on the basis of existing taxation. The new taxation proposals, which are expected to yield Rs. 20.1 crores, are as follows :

(1) A central surcharge on taxes on income above Rs. 5,000 per annum which amounts uniformly to 66 $\frac{2}{3}$ per cent. over the basic rates of Income-tax ; (2) Increase in Super-tax on slabs between Rs. 25,000 and Rs. 3 $\frac{1}{2}$ lakhs by uniform half an anna ; (3) Rise in Corporation Tax to two annas in the rupee ; (4) Indirect taxation includes excise on tobacco and vegetable products ; Tobacco grown for personal consumption of grower or his household is exempted from excise duty ; (5) Further increases in postal and telephone rates. The Finance Member also announced that the balance of the deficit will be met by borrowing.

The portion of the speech of the Finance Member relating to direct taxation is as follows :

“ It remains for me finally to lay before the House the proposals of the Government for dealing with the revenue deficit of Rs. 60.29 crores which, on the estimates I have presented, is anticipated in the forthcoming financial year. We have also in this context, to bear in mind that the current year will, it is estimated, close with a revenue deficit of Rs. 94.66 crores. By far the larger part of these sums has, of course, to be met by borrowing, but it is proposed to raise Rs. 20 crores or approximately one-third of the prospective deficit, by new taxation. Last year, we introduced into our system of direct taxation certain features which combined the methods of borrowing and taxation. Whilst such experience as we have had justifies the retention of these features, it is not proposed to endeavour to extend their scope further this year. The reasons are not far to seek.

“ The incomes which come within the orbit of our income-tax system are those of a comparatively small fraction of the population, a section in which, moreover, the habit of investment in public loans is generally speaking already well established. It is impossible to deal adequately with the problem of surplus purchasing power by methods which do not touch agricultural income at all and which are inapplicable to that vast body of industrial employees, whose incomes fall below any taxable minimum which it is practicable to adopt. It is, therefore,

clear that the national savings movement must cast its net far more widely and must secure the co-operation of large elements in the country, who are not affected by direct taxation. Whilst action on these lines thus calls for unremitting attention and a constantly renewed endeavour, it will not affect our immediate proposals.

"To deal first with income-tax, there will be no change in regard to incomes up to Rs. 5,000. On the next slab of incomes from Rs. 5,000 to Rs. 10,000, the central surcharge will be increased from nine pies to ten pies in the rupee, and on the slab from Rs. 10,000 to Rs. 15,000, it will be raised from fourteen to sixteen pies in the rupee, on the balance above Rs. 15,000 the surcharge will be increased from fifteen to twenty pies in the rupee. The effect of these changes will be to impose a surcharge amounting uniformly to 66⅔ per cent. over the basic rates of income-tax. At the same time, there will be an increase in the super-tax on the slabs of income between Rs. 25,000 and Rs. 3½ lakhs: here the surcharge will be raised uniformly by half an anna in the rupee. The resultant aggregate rate of super-tax, including surcharge, will thus run from two annas in the rupee on the lowest slab to ten and a half annas on the top slab. Corporation Tax will also be raised by half an anna, to a rate of two annas in the rupee. The Excess Profits Tax will be extended to cover the profits of a further period of one year, but the rate of 66⅔ per cent will remain unchanged. The additional revenue from these changes in direct taxation is estimated at Rs. 7 crores in the coming year."

INCOME TAX ESTABLISHMENTS.

Notification No. 1-D dated the 6th February 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendments shall be made, in its notification No. 19 Income-tax, dated the 1st April 1939, namely:—

In the Schedule annexed to the said notification—

(i) for the entries in columns 4 and 6 against Serial Nos. 42 and 48, the following entries, respectively, shall be substituted, namely:—

"Inspecting Assistant Commissioner of Income-tax, Amritsar Division"

"Commissioner of Income-tax, Punjab and N.W.F. Provinces."

(ii) for the entries in columns 4 and 6 against Serial No. 44, the following entries, respectively, shall be substituted, namely:—

"Inspecting Assistant Commissioner of Income-tax, Delhi."

"Commissioner of Income-tax, Delhi Province."

(iii) for the entry in column 6 against Serial No. 49, the following entry shall be substituted, namely:—

"Commissioner of Income-tax, Punjab and N.W.F. Provinces."

(iv) for the entries in column 5 against Serial Nos. 51 and 51-A, the following entries respectively, shall be substituted, namely:—

"Appellate Assistant Commissioner of Income-tax, Rawalpindi Range."

"Appellate Assistant Commissioner of Income-tax, Lahore Range."

[The amendments at (i), (ii) and (iii) above shall take effect from the afternoon of the 21st September 1942, and the amendment at (iv) above, from the 1st December 1942.]

Notification No. 2-D dated the 6th February 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), as applied to the Hyderabad Administered Areas, the Central Board of Revenue directs that, with effect from the afternoon of the 21st September 1942, the following amendments shall be made in its notification No. 2-D-Income-tax, dated the 2nd March 1940, namely :—

In the Schedule annexed to the said notification, against Serial No. 5—

(i) in the entry in column 4, the word "Division" shall be omitted;

(ii) for the entry in column 6, the following entry shall be substituted, namely :—

"Commissioner of Income-tax, Delhi Province."

Notification No. 2 dated the 23rd January 1943.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that, with effect from the 1st February 1943, the following further amendment shall be made in the Schedule appended to its Notification No. 58-Income-tax, dated the 15th July 1939, namely :—

In the said Schedule under the sub-head "IV—United Provinces and Central Provinces and Berar—" for the Ranges "Lucknow", "Agra" and "Benares" and the Income-tax circles specified against them, the following Ranges and Income-tax circles shall be substituted, namely :—

Lucknow—

- (1) Lucknow.
- (2) Benares.
- (3) Azamgarh.
- (4) Gorakhpur.
- (5) Fyzabad.
- (6) Gonda.
- (7) Sitapur.
- (8) Bareilly.

Agra—

- (1) Agra.
- (2) Jhansi.
- (3) Farrukhabad.

(4) Aligarh.

- (5) Meerut.
- (6) Military Circle, Meerut.
- (7) Saharanpur.
- (8) Dehra Dun.
- (9) Moradabad.

Cawnpore—

- (1) Cawnpore.
- (2) Special Income-tax cum Excess Profits Tax Circle, Cawnpore.
- (3) Allahabad.
- (4) Central Circle, Allahabad.

EXCESS PROFITS TAX ESTABLISHMENTS.

Notification No. 1 dated the 23rd January 1943.

In exercise of the powers conferred by sub-section (3) of Section 3 of the Excess Profits Tax Act, 1940 (XV of 1940), the Central Board of Revenue hereby directs that, with effect from the 1st February, 1943, the following further amendment shall be made in its Notification No. 33-C. A.-Excess Profits Tax Establishments, dated the 14th September, 1940, namely:—

In the Schedule appended to the said notification, for item 3, the following item shall be substituted, namely:—

- | | | |
|--------------------------------------------------------------------------------------------------------------------------------------|---|-------------------------------------------------------|
| <p>“3. The person performing, for the time being, the functions of Appellate Assistant Commissioner of Income-tax, Cawnpore.</p> | } | <p>3. All cases in the United Provinces.”</p> |
|--------------------------------------------------------------------------------------------------------------------------------------|---|-------------------------------------------------------|

EXCESS PROFITS TAX RULES, 1940—AMENDMENT TO.

Notification No. 1 dated the 20th February 1943.

In exercise of the powers conferred by Section 27 of the Excess Profits Tax Act, 1940 (XV of 1940), the Central Board of Revenue directs that the following further amendment shall be made in the Excess Profits Tax Rules, 1940, the same having been previously published as required by sub-section (3) of the said section, namely:—

To the said Rules, the following rule shall be added, namely:—

“20. *Investment holding Companies.*—In the case of a business consisting wholly or mainly in the holding of investments—

(a) the income from investments to be included in the profits of the business under the provisions of Rule 4 of Schedule I to the Act shall be computed exclusive—

(i) of all income received by way of dividends or distribution of profits from a company carrying on a business to the whole of which the section of the Act imposing excess profits tax applies; and

(ii) of the due proportion of all income received by way of dividends or distribution of profits from a company carrying on a business to part only of which the section of the Act imposing excess profits tax applies;

(b) the investments to be excluded from the capital employed in the business under Rule 3 of Schedule II to the Act shall include—

(i) all shares in a company carrying on a business to the whole of which the section of the Act imposing excess profits tax applies; and

(ii) the due proportion of all shares in a company carrying on a business to part only of which the section of the Act imposing excess profits tax applies.”

Notification Applying Income-tax Proceedings Validity

Ordinance, 1943, to British Baluchistan.

Notification No. 19 W dated the 10th February 1943.

In pursuance of sub-section (2) of Section 95 of the Government of India Act, 1935, the Governor-General in his discretion is pleased to direct that the Income-tax Proceedings Validity Ordinance, 1943, (Ordinance No. IV of 1943) shall apply to British Baluchistan.

Income Tax Reports.

VOLUME XI—PART VI.

NOTES AND COMMENTS.

Assessment of Hindu Undivided Families After Partition : Sec. 25 A.

EARLIER CASES.

An important question affecting the assessment of Hindu undivided families was set at rest by the Privy Council in *Sir Sunder Singh Majithia's case* [1942] (10 I.T.R. 457) in accordance with the views which we had expressed. We are much gratified to find that another question of every day importance affecting Hindu undivided families upon which there is much conflict of opinion in India is also taking a turn in the right direction. When the Full Bench of the Lahore High Court decided in *Sher Singh Nathuram's case* [1934] (2 I.T.R. 479) that in order to satisfy the provisions of Section 25A of the Income-tax Act and to entitle the members of a Hindu joint family to be assessed as separate units, a division in status with ascertainment of their shares was sufficient, we expressed our agreement with the earlier decision of Addison & Sale, JJ., to the contrary in *Saligram Ramlal's case* and our disagreement with the Full Bench decision in the following terms.

OUR COMMENTS IN [1934] (2 I.T.R. pp. 76-77).

The grounds on which the Full Bench have based their opinion are: *first*, that Section 25A itself 'recognises co-ownership and does not hold that a Hindu joint family must split into its individual components before it can be said that the family has partitioned its property within the meaning of the section.' But this is certainly not inconsistent with a further provision that if the co-owners want to be assessed *as separate units*, there must be a partition between them of their property in definite portions. It is equally difficult to follow the second ground, namely, that the property owned by a family may be a trading business and that nothing more could be done to such business except to ascertain the shares. We doubt, further, whether their Lordships are right in taking the word 'portion' as identical in meaning with 'share.' We use the word 'portion' to denote a physical tangible part of a thing and the word 'share' to denote an abstract fractional share, *e.g.*, we say 'a portion of the land was washed away' or a 'portion of a house is to let.' We do not use 'share' in such cases. The word 'partition' itself in its ordinary sense means division

of the property between co-owners and not mere conversion of coparcenary into a co-ownership. When we direct our attention to the wording of Section 25A and to the exact significance of the words 'partitioned,' 'definite' and 'portions,' we have to say with Addison and Sale, JJ., that it is impossible to construe the words 'property has been partitioned.....in definite portions' in Section 25A as referring to anything other than a partition by metes and bounds, that is, a division of the joint family property into specific portions and not merely into abstract fractional shares. To make the point clearer, if two co-sharers *A* and *B* decide to separate, and merely say that each is entitled to a half share in the abstract in the common property, we cannot say there has been a partition of their property in definite portions. But if they say that the eastern half of the property belongs to *A* and the western half to *B*, or that items *X*, *Y* and *Z* are allotted to *A*, and *P*, *Q* and *R* to *B*, though the marking out of the items and delivery of possession may take place later on, there is a partition of the property in definite portions. And this, we think, is what is required for the purposes of Section 25A."

RECENT BOMBAY CASE.

The Bombay High Court has now in an elaborate judgment considered this question in *Gordhandas T. Mangaldas v. Commissioner of Income-tax, Bombay* (reported *infra* at p. 183). They have also dissented from the Lahore Full Bench Case and agreed with the opinion of Addison & Sale, JJ. From a perusal of the judgment of the Bombay High Court it will be seen that our comments on the Lahore Full Bench case were quite justified.

A WORD OF CAUTION.

Before leaving this topic, however, we wish to observe that it is not correct to lay down broadly that a 'physical division' or a 'division by metes and bounds' is necessary to satisfy Section 25A. We should not erase the words 'partitioned in definite portions' which have been advisedly used by the Legislature and paste over them the words 'partitioned by metes and bounds' or 'divided physically,' because it is clear that it may be possible in several cases 'to define the portions' without a partition by metes and bounds or physical division, that is, without any change or mark in the physical condition of the properties. The illustration pointed out in the last portion of our comment cited above makes this point clear. The exact position is this: (i) severance of status even if accompanied by ascertainment of shares is not enough, (ii) a division into definite portions is necessary, (iii) but a physical division or partition by metes and bounds involving any tangible alteration or mark in the physical condition of the properties is unnecessary.

EXCESS PROFITS TAX AND WAR DAMAGE.

A question of considerable importance to excess profits tax payers was raised in the United Kingdom (House of Commons) when an honourable member brought up a new clause* to the Finance Bill, 1942, which dealt with war damage in relation to excess profits tax. Sir Kingsley Wood (The Chancellor of the Exchequer) explained the law and practice in relation to the incidence of excess profits tax where business assets have been destroyed or lost owing to enemy action and assured the House that he would consider the whole matter once again, and then the clause was by leave, withdrawn.

The speech of Sir Kingsley Wood which is printed at page 970 of the Parliamentary Debates, Fifth Series, Volume 380, runs as follows:

“The honourable Member for the Attercliffe Division (Mr. Wilson) has raised a matter of considerable importance to a number of people. It will be appreciated that I could not insert a clause of this kind in the Bill. If any alterations were to be made, they would have to be of a specific character. However, the new clause does give me an opportunity of stating the law and practices concerning this matter, on which there is, I think, a certain amount of misapprehension. I should like to explain, in the first place, the existing practice in relation to the incidence of Excess Profits Tax in cases where business assets have been destroyed or lost owing to enemy action. My right honourable Friend, the Member for East Edinburgh (Mr. Pethick-Lawrence) will recollect that the Excess Profits Tax takes as its measure of charge the excess of current profit over the profit earned in the pre-war years. Where the pre-war profit was abnormally low, the datum line is fixed by reference to the capital employed in the business in the pre-war years, and generally comes out at 6 per cent. of the amount of that capital.

The first principle of the tax is the principle of comparison of like with like. It is only in so far as the capital employed in a business is the same today as it was in the pre-war years that it would be reasonable to measure the Excess Profits Tax by comparing the present profits with pre-war profits, or with the percentage of pre-war capital. Where a business has expanded by reason of additional capital being employed in it, the pre-war standard is increased by 8 per cent.

* The clause introduced in the Finance Bill, 1942, and which was subsequently withdrawn runs as follows :—

“Notwithstanding anything in the enactments relating to excess profits tax the Commissioners may make regulations to provide that where any trade or business suffers a loss of capital through enemy action the amount of excess profits tax payable shall be adjusted to ensure that the person carrying on the trade or business shall not be in a worse financial position than he would have been had there been no such loss.”

on the increase of capital, and, similarly, where capital is no longer employed in a business, it is necessary to adjust the pre-war standard; accordingly the law provides that, where there is a fall in capital employed, a deduction of the standard profits is to be made on an amount representing 6 per cent. of the fall in the capital. That is the general position for the treatment of an increase or a decrease in capital employed in a business and the provisions are to be found in the Finance (No. 2) Act, 1939, which first imposed the Excess Profits Tax.

Now I should like to refer to the particular case to which my hon. Friend has called attention to-day—that is the loss of capital due to enemy action. I must emphasise that we are concerned to-day only with the incidence of the Excess Profits Tax in such a case, and that compensation for loss suffered owing to enemy action is a different matter with which at this moment we are not expressly concerned. Where capital represented by trading assets has been destroyed by enemy action or has been temporarily lost owing to seizure by enemy action, the capital so destroyed or so lost is no longer employed in the business, and the provisions of the law relating to a deduction of capital employed in the business are, therefore, applicable in all these cases. Take, for example, a shipping company with a fleet of 12 ships of which 6 have been lost owing to enemy action. In computing the excess profits for the six ships remaining in service, it would not be reasonable to take the pre-war standard representing the standard of profit of running 12 ships; accordingly that standard has to be reduced to 6 per cent. of the value of the six ships which have been sunk. The loss suffered in respect of the sunk ships is a question of compensation which is covered by the insurance monies, and I may observe that any interest earned or accruing on such monies is outside the scope of the Excess Profits Tax.

Take the case which has been put today. Take a concern which has two factories, one of which has been completely destroyed. The standard for the measurement of the excess profits for the remaining factory cannot be taken to be the standard applicable to the two factories, and an abatement has to be made in respect of the loss of capital represented by the destroyed factory. But, in applying its provisions one has to bear in mind the principle of comparing like with like, to which I have already referred, and in practice, the application of this principle is directed to ensuring that the pre-war standard is only reduced where it is clear that the loss of capital has resulted in a corresponding fall in productive or profit-earning capacity. No regard is paid, therefore, to partial damage to trading assets, such as the damage to a wing of a factory, or partial damage to trading

premises which still continue to be used for the purposes of trade. In general, where it is shown that the business has been carried on without any material impairment of its productive or profit-earning capacity, no deduction from the standard would be made in respect of any capital which may have been lost or destroyed.

A good example of this kind is to be found in the cotton industry. In that industry all the looms are not fully employed, and in certain cases a good neighbours arrangement exists under which the owner of a mill which may be destroyed by enemy action can take over the unused looms in another mill and carry on his normal production. The revenue authorities have agreed with the cotton industry that in such cases the standard of the concern whose mill was destroyed will not be reduced by reason of the destruction of the mill. A further example, which may be of general interest, is the case where the premises of a trading concern engaged in the distributive trade whose shops or stores in the centre of our blitzed cities may have been destroyed. Where such a concern takes over other premises and carries on its business so that the profit-earning capacity remains substantially unchanged, no reduction will be made for capital lost, which would have the effect, taking into account such rent as may be paid for the new premises, of increasing the measure of the liability to excess profits tax. That sets out the practice, and, of course, a statement of this kind requires careful consideration by those who desire to read and examine it. On the whole, I think that it represents a fair application of the principles of the law.

The clause which stands in the name of my hon. Friend the Member for Attercliffe does not deal with a question that has sometimes been raised, and has again been put to me by my hon. Friend the Member for South Kensington (Sir W. Davison). I would say in reply to him that, if a trader has a stock of whisky worth, say, £100,000 and the stock is destroyed, he receives under the Government's insurance scheme £100,000; and is treated for taxation purposes in the same way as if he had sold the whisky across the counter for £100,000. The profit arising on the sale is taxed, and so is the profit arising on the payment for whisky stock which has been destroyed. The fact that a trader has to find finance for acquiring new stocks does not affect the liability to taxation, whether new stocks are rendered necessary by ordinary sales or by compulsory sales which is the resultant effect of the destruction.

Sir W. Davison: The trader would not wish to sell £100,000 worth of whisky. He could not replace it. Everyone who is in the habit of buying whisky knows that you can only buy one bottle when

before you might have been accustomed to buy a dozen. It means that the business is ruined. I stated in my speech that it means ruining the business and putting it out of action, because a trader cannot in present circumstances replace the stuff which has been destroyed. His business is, therefore, closed down. It is not the same thing to say that he could have sold £100,000 worth of whisky on the market and that he has received £100,000 from the War Damage Commission and, therefore, he ought to be very well pleased, because he is getting a quick sale.

Sir K. Wood: I will examine that case again. It has only just been dealt with. As a matter of fact, it is not dealt with so far as this clause is concerned, and I hope that my hon. Friend will, in the circumstances, be satisfied with the explanation I have given.

Mr. Wilson: There is the case where premises are temporarily destroyed and for a long period no business is carried on.

Sir K. Wood: That will be another matter, I agree.

Mr. Wilson: Will it be looked into?

Sir K. Wood: Certainly.

Sir W. Davison: Will my right hon. Friend look into the whole question and see what can be done?

Sir K. Wood: I think I have given a very fair statement of the position generally. I will examine the whole matter."

The question was again raised in the House on August 4, 1942, when the Chancellor of Exchequer expressed his inability to alter the law. The question and Sir Kingsley Wood's answer thereto are printed below.

Sir W. Davison asked the Chancellor of the Exchequer whether he has now been able to look into the case, to which his attention has been drawn, where the Inland Revenue has been treating payments by the War Damage Commission in respect of stock destroyed by enemy action as a constructive sale, the profits of which are liable to Excess Profits Tax, notwithstanding the fact that the whole of such payments are required for the replacement of the stock destroyed; and what action it is proposed to take to deal with cases of this kind?

Sir K. Wood: I have carefully considered the case to which my hon. Friend refers, and I regret I cannot see my way to propose any alteration of the law under which payments received in compensation for destroyed trading stocks, in common with insurance payments or payments that may be made for compulsory acquisition of trading stocks, fall to be included as trading receipts for the purpose of computation of trading profit.

Sir W. Davison : Does not my right hon. Friend realise that the Treasury's interpretation of the law, in treating a payment by the War Damage Commission as a constructive sale, means the ruin of many old established businesses? That was never intended to be the result of the Excess Profits Tax and, when the matter was discussed on 9th June, all parties, including the late Financial Secretary to the Treasury, urged that this inequity should not continue?

Sir K. Wood : I could not assent to all that my hon. Friend has said. He has given me one case in which I regret that there are certain circumstances which make for a degree of hardship, but I do not think I could propose an alteration in the law.

Sir W. Davison : That is only an example of many other cases, and, even if there is only one case, why should one man be unjustly treated?

INCOME TAX ESTABLISHMENTS.

Notification C. No. 50-G. I. (1) I.T./43 dated the 6th March 1943.

Under sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs, in supersession of its Orders C. No. 50-Gl. (10)-I.T./42, dated the 14th August 1942 and C. N. 50-Gl. (28)-I.T./42, dated the 13th November 1942, that for such period as an Additional Appellate Assistant Commissioner of Income-tax is appointed to the Nagpur Range, the distribution and allocation of work to be performed between the Additional Appellate Assistant Commissioner of Income-tax and Appellate Assistant Commissioner of Income-tax of that Range shall be as follows, namely :—

The Additional Appellate Assistant Commissioner of Income-tax shall have his headquarters at Nagpur and perform his functions in respect of all persons and income assessed to income-tax or super-tax in the income-tax circles specified below :—

(1) Central Salary Circle, Nagpur, (2) Jubbulpore circle, (3) Saugor circle, (4) Khandwa circle, (5) Chhindwara circle, (6) Raipur circle, (7) Akola circle, and (8) Wardha circle.

The Appellate Assistant Commissioner of Income-tax shall perform his functions in respect of all persons and incomes assessed to income-tax or super-tax in the remaining income-tax circles in the Nagpur Range :

Provided that the Appellate Assistant Commissioner of Income-tax, shall also, and the Additional Appellate Assistant Commissioner of Income-tax, shall not, perform his functions in respect of such persons or income assessed to income-tax or super-tax in the eight

income-tax circles allocated to the Additional Appellate Assistant Commissioner of Income-tax and in respect of which Mr. K. C. Avashia exercised the powers of Inspecting Assistant Commissioner of Income-tax, Central Provinces and Berar.

On the Additional Appellate Assistant Commissioner of Income-tax for the Nagpur Range ceasing to perform his functions, the Appellate Assistant Commissioner of Income-tax for that Range shall perform his functions in respect of all persons and incomes assessed to income-tax or super-tax in the income-tax circles in the Nagpur Range.

2. This order shall take effect from 15th March 1943.

INCREASE IN INCOME TAX AND EXCESS PROFITS TAX.

The following passages in the recent Budget speech of the Finance Member give an idea of the increase in income-tax and excess profits tax and the total revenue derived from these taxes :—

1942-43 : Collections of Income-tax and Corporation Tax have continued to increase. Receipts on account of ordinary Income-tax including central surcharge are expected to yield Rs. 7 crores more than our Budget estimates. With increasing experience gained in the administration of the Excess Profits Tax Act, the work of assessment has steadily progressed and our total collections under this head, including advance payments, are expected to reach Rs. 26 crores, that is Rs. 7 crores more than the Budget estimate. The provincial share of the divisible pool of Income-tax will now be approximately Rs. 10·55 crores as against Rs. 8·37 crores originally provided for in the budget.

1943-44 : As regards Corporation tax and other taxes on income, including Excess Profits Tax, we have, after taking into account the trend of our recent collections and making allowance for the assessments yet to be made, raised our estimate of the total yield from these taxes by Rs. 17 crores. Of a total of Rs. 95 crores estimated under these two heads of revenue, Excess Profits Tax alone is expected to yield Rs. 40 crores. The divisible pool of Income-tax has been taken as Rs. 33·19 crores and the share available to Provinces will be even better than in the current year, touching the record figure of Rs. 12·10 crores.

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VOLUME XI—PARTS VII & VIII.

NOTES AND COMMENTS.

Payment to Employee for Not Competing After Termination of Service.

We would invite the attention of directors of companies to the important decision of the House of Lords in *Beak v. Robson* (to be reported shortly). Covenants not to compete with the employer after termination of service are very common in contracts of service and failure to observe the principle laid down by the House of Lords in this case may lead to the payment of tax on receipts which are not really taxable. The facts of the case were as follows:—

The assessee entered into an agreement with a company whereby he was to be employed for a term of five years as director and manager at a salary therein stated. The agreement contained clauses under which in the event of the assessee determining the agreement by notice, as he was entitled under one of its clauses to do, or committing a breach of it which led to a determination, he covenanted for a stated period, not to be engaged or interested in the business of a coal exporter within a radius of 50 miles of Newcastle-upon-Tyne without the consent of the company. In consideration of his entering into that covenant the assessee was paid a sum of £ 7,000. The question was whether this sum was assessable to income-tax as remuneration from the office of director and manager.

The House of Lords unanimously held, affirming the Court of Appeal, that the amount was not so taxable. The Lord Chancellor, fully agreeing with the judgment of Lord Greene, M. R., observed as follows:—"In the agreement before us, the obligations flowing from the contract of service and the remuneration to be received by the respondent in respect of that service are entirely separate from the restrictive covenant and the consideration which is given for it. The sum of £ 7,000 is not paid for anything done in performing the services in respect of which Robson is chargeable under Schedule E. The consideration which he has to give under the covenant is to be given not during the period of the employment but after its termination. He is giving to the company for a sum of £ 7,000 the benefit of a covenant which will only come into effect when the service is concluded. I agree with the Court of Appeal in the view that to treat this £ 7,000 as a profit arising from the respondent's office is to ignore the real nature of the transaction. It is quite true that, if he had not entered into the agreement to serve as a director and manager, he would not have received £ 7,000. But that is not the same thing as

saying that the £ 7,000 is profit from his office of director so as to attract tax under Schedule E."

Restrictive covenants are commonly found in managerial agreements without there being any consideration separately allocated to them. In such cases, the Attorney-General asked, whether the decision has not the effect of apportioning the remuneration received under the agreement between the profit from office and the price paid to secure the covenant. The Lord Chancellor did not express any opinion on this aspect of the case. Their Lordships had however no doubt that if the covenant is severable from the other terms of the contract and if the consideration in respect of the obligations under the covenant is separate, then the consideration paid in respect of the covenant cannot be said to be remuneration for the service and cannot therefore be taxed.

Directors of companies would be well advised in remembering this decision in drafting service agreements. It is not very difficult to sever the consideration for the restrictive covenant from the main consideration or remuneration for service.

Discontinuance of Business Assessed Under the Act of 1918.

It was held by the Bombay High Court in *P. E. Polson, In re* (1942, 10 I.T.R. 52) that the word 'discontinued' in Section 25 (3) of the Income-tax Act as amended in 1939 covers a discontinuance either by cessation or by disposal and that therefore an assessee who assigned his business taxed under the 1918 Act on the 1st of January 1939 to a limited company was entitled to the benefit of Section 25 (3) in the assessment year 1939-40. In commenting upon this decision in the *Company Cases* we wrote as follows (1942) (12 Comp. Cas. Notes and Comments 11) :—

"It is true that hardship will be caused to the assessee if he is not given relief and it is just and equitable that he should be given relief. But that is no justification for changing the meaning of a word which has a long established meaning. The interpretation put upon the word "discontinued" by the learned Judges is not only contrary to the ordinary meaning of the word but is also not warranted by the section. Section 25 (3) speaks of discontinuance of business, profession or vocation and not of discontinuance of business, profession or vocation by the assessee. It is not proper to read the word "discontinued" as relating to the assessee. If the section contains the words "by the assessee" after the word "discontinued," then the view of the learned Judges would have been quite correct. In our opinion *discontinuance* mentioned in the section is a total or absolute cessation of the business and not a discontinuance in the sense of its ceasing to

be carried on by a proprietor who passes it on to another who continues it. Moreover, if discontinuance includes a transfer, then where is the necessity for Section 25 (4)? All cases coming under Section 25 (4) would then come under Section 25 (3) and Section 25 (4) becomes redundant. The word "discontinued" has acquired a meaning which has not been challenged in any Court of law for a number of years and consequently if the legislature intended to change its meaning they would have certainly introduced a provision in the Act when it was amended in 1939 to the effect that "discontinued" also covers a discontinuance by disposal. Though the interpretation given to 'discontinuance' in the judgment of the Bombay High Court prevents an injustice in a particular set of circumstances, we fear this interpretation is too wide and may lead to unexpected complications."

It is a matter of much gratification to us that in the recent case of *Meyyappa Chettiar v. Commissioner of Income-tax, Madras* (reported *infra*), the Madras High Court has dissented from the decision of the Bombay High Court and endorsed our view. The Judges held without hesitation that the word 'discontinued' in Section 25 (3) means cessation and does not cover cases of succession and therefore where a Hindu undivided family carrying on business which was taxed under the 1918 Act becomes disrupted and the members continue the business thereafter as partners the provisions of Section 25 (3) do not apply.

'Appointment' of Income-tax Authorities.

The decision of the Bombay High Court in *Gobindram Seksaria, In re*, (1943, 11 I.T.R. 104) that there is no valid 'appointment' as an Income-tax Officer where an Assistant Income-tax Officer is appointed 'to perform the functions of an Income-tax Officer' has led to the passing of the Income-tax Proceedings Validity Ordinance, 1943. While the principle of the decision applies to the appointment of all Income-tax authorities including Commissioners and Assistant Commissioners, the Ordinance applies only to the appointment of Assistant Income-tax Officers to perform the functions of Income-tax Officers. Occasions are sure to arise when it may be necessary to appoint Income-tax Officers to perform the functions of Assistant Commissioners and to appoint Assistant Commissioners to perform the duties of Commissioners. Though we wholly disagree with the view of the Bombay High Court on this point—in particular, with the observation of the Chief Justice that an assessee is entitled to say that he can only be assessed by somebody who is on the relevant date in the grade of Income-tax Officer and that he cannot be assessed by somebody who is not in that grade but is merely appointed to perform the functions

of an officer of that grade—we think, now that there is this decision before us, that a comprehensive provision applicable to the appointment of Income-tax Officers, Assistant Commissioners, and Commissioners is necessary. The addition of a small paragraph in Section 5 of the Income-tax Act or of the words ‘or to perform the functions of’ in clauses (5), (6D), and (7) of Section 2 would prevent unexpected complications in assessment and the necessity of passing Ordinances for such small matters.

THE INDIAN INCOME-TAX (AMENDMENT) BILL, 1943.

A Bill further to amend the Indian Income-tax Act, 1922.

Whereas it is expedient further to amend the Indian Income-tax Act, 1922 (XI of 1922), for the purpose hereinafter appearing ;

It is hereby enacted as follows:—

1. *Short title and commencement.*—(1) This Act may be called the Indian Income-tax (Amendment) Act, 1943.

(2) It shall come into force at once.

2. *Amendment of Section 30 (1), Act XI of 1922.*—In sub-section (1) of Section 30 of the Indian Income-tax Act, 1922 (XI of 1922), after the words and comma “or denying his liability to be assessed under this Act,” the following shall be inserted:—

“or denying his liability to make or to have made a deduction under Section 18.”

3. *Amendment of Section 30 (2), Act XI of 1922.*—In sub-section (2) of Section 30 of the Indian Income-tax Act, 1922 (XI of 1922), after the words “thirty days” the following shall be inserted:—

“of an intimation from an Income-tax Officer that a person should deduct or should have deducted tax under any of the provisions of Section 18, or.”

4. *Amendment of Section 31, Act XI of 1922.*—In sub-section (3) of Section 31, after sub-clause (g) the following shall be inserted:—

“or, in the case of an appeal from an intimation from an Income-tax Officer that a person should deduct or should have deducted tax under any of the provisions of Section 18,

(h) confirm, cancel or vary such intimation.”

STATEMENT OF OBJECTS AND REASONS.

The Indian Income-tax Act deems a person who fails to deduct tax in accordance with the provisions of Section 18 to be an assessee in default with the consequences that he becomes liable to make the payment of tax and may be subjected to a penalty. The Act gives him no right of appeal where he disputes his liability to make a deduction. Income-tax Officers who consider that a deduction should be made or should have been made, so intimate with the threat of penalty. The Act contains no machinery by which a person who receives such an intimation and who has been advised or considers he is not liable to deduct tax can have the dispute adjudicated upon. It is therefore necessary to provide such machinery by giving any such person a right of appeal.

Income Tax Reports.

VOLUME XI—PARTS X & XI.

EXCESS PROFITS TAX ORDINANCE 1943.*

ORDINANCE No. XVI OF 1943.

An Ordinance

to make certain provisions in connection with the tax on excess profits.

Whereas an emergency has arisen which renders it necessary to make certain provisions in connection with the tax on excess profits;

Now, therefore, in exercise of the powers conferred by Section 72 of the Government of India Act, as set out in the Ninth Schedule to the Government of India Act, 1935 (26 Geo. 5, c. 2), the Governor-General is pleased to make and promulgate the following Ordinance:—

1. *Short title, extent and commencement.*—(1) This Ordinance may be called the Excess Profits Tax Ordinance, 1943.

(2) It extends to the whole of British India.

(3) It shall come into force at once.

2. *Deposits in connection with payments of excess profits tax.*—

(1) When excess profits tax charged under the provisions of the Excess Profits Tax Act, 1940 (XV of 1940), in respect of any chargeable accounting period ending after the 31st day of December, 1942, becomes payable under that Act after assessment made under Section 14 of that Act, the person liable to pay such excess profits tax shall deposit with the Central Government, before such date as may be specified in a notice in this behalf in such form as may be prescribed by rules made under sub-section (5) issued to him by the Excess Profits Tax Officer, a further sum equal to one-fifth of the amount of the said excess profits tax; and the provisions of Section 10 of the Indian Finance Act, 1942 (XII of 1942), shall, save in so far as they are inconsistent with this section, apply in respect of such deposits as they apply in respect of the voluntary deposits for which provision is made in the said Section 10.

(2) The provisions of sub-section (1) of Section 10 of the Indian Finance Act, 1942 (XII of 1942), in so far as they enable the making of voluntary deposits, shall cease to have effect except in relation to excess profits tax charged in respect of a chargeable accounting period ending on the 31st day of December, 1942, or earlier.

(3) Any further sum such as is referred to in sub-section (1) deposited in accordance with that sub-section shall be repaid by the Central Government within twelve months of the date of termination of the present hostilities or within twenty-four months of the date on which the deposit was made, whichever is later.

* Published in the Gazette of India Extraordinary dated May 17, 1943.

(4) The provisions of law applicable to the payment and recovery of excess profits tax contained in Sections 45 and 46 [except sub-sections (1) and (1A) thereof] of the Indian Income-tax Act, 1922 (XI of 1922), as applied by Section 21 of the Excess Profits Tax Act, 1940 (XV of 1940), shall apply to the payment and recovery of the deposits required by sub-section (1) of this section as if the notice referred to in sub-section (1) of this section were a notice of demand under Section 29 of the Indian Income-tax Act, 1922 (XI of 1922), and as if a default in making payment of such deposit were a default in making payment of excess profits tax.

(5) The power to make rules for carrying out the purposes of Section 10 of the Indian Finance Act, 1942 (XII of 1942), conferred by sub-section (3) of that section shall include a power to make rules for carrying out the purposes of this section.

3. *Insertion of new Section 14A in Act XV of 1940.*—After Section 14 of the Excess Profits Tax Act, 1940 (XV of 1940), the following section shall be inserted :—

“14A. *Power to make provisional assessments.*—(1) The Excess Profits Tax Officer, before proceeding to make an assessment (in this section referred to as the regular assessment) under Section 14, may, at any time after the expiry of the period specified in the notice issued under sub-section (1) of Section 13 as that within which the return therein referred to is to be furnished, and whether the return has or has not been furnished, proceed to make in summary manner a provisional assessment of the amount by which the profits of the chargeable accounting period exceed the standard profits, and the amount of excess profits tax payable thereon.

(2) Before making such provisional assessment the Excess Profits Tax Officer shall give notice in the prescribed form to the person on whom assessment is to be made of his intention to do so, and shall with the notice forward a statement of the amount of the proposed assessment, and the said persons shall be entitled to deliver to the Excess Profits Tax Officer at any time within fourteen days of receipt of the said notice a statement of his objections, if any, to the amount of the proposed assessment.

(3) On expiry of one month from the date of service of the notice referred to in sub-section (2), or earlier if the assessee agrees to the proposed assessment, the Excess Profits Tax Officer may, after taking into account the objections, if any, made under sub-section (2), make a provisional assessment, and shall furnish a copy of the order of assessment to the assessee :

Provided that assent to the amount of the assessment, or failure to make objection to it, shall in no way prejudice the assessee in relation to the regular assessment.

(4) In making any such provisional assessment the Excess Profits Tax Officer shall make allowances for any deficiencies of profits for previous chargeable accounting periods which are under the provisions of Section 7 to be set off against the excess profits of the chargeable accounting period in respect of which the assessment is being made :

Provided that where such deficiencies of profits have not been determined under sub-section (1) of Section 14 the Excess Profits Tax Officer shall estimate the amount thereof to the best of his judgment.

(5) There shall be no right of appeal against a provisional assessment made under this section, and it shall, until a regular assessment is made in due course under Section 14, determine the amount of excess profits tax due from the assessee.

(6) If, when a regular assessment is made in due course under Section 14, the amount of excess profits tax payable thereunder is found to exceed that determined as payable by the provisional assessment, it shall be reduced by the amount determined as payable by the provisional assessment.

(7) If, when a regular assessment is made in due course under Section 14, the amount of excess profits tax payable thereunder is found to be less than that determined as payable by the provisional assessment, any excess of tax paid as a result of the provisional assessment shall be refunded to the assessee together with interest at 5 *per cent. per annum* calculated from the date of payment of such excess tax to the date of the order of refund, both days inclusive."

4. *Amendment of rule 12, Schedule I, Act XV of 1940.*—In the First Schedule to the Excess Profits Tax Act, 1940 (XV of 1940), to rule 12 the following sub-rule shall be added, namely:—

"(3) In relation to chargeable accounting periods ending after the 31st day of December, 1942, the Central Government may make rules for determining the extent to which deductions shall be allowed in respect of bonuses or commissions paid."

5. *Amendment of rule 3, Schedule II, Act XV of 1940.*—In the Second Schedule to the Excess Profits Tax Act, 1940 (XV of 1940), rule 3 shall be renumbered as sub-rule (1) of rule 3 and—

(a) in the rule as so re-numbered after the words "any moneys" the words "or as regards any chargeable accounting period ending after the 31st day of December, 1942, any trading stock or stock of raw materials" shall be inserted;

(b) the following shall be added as sub-rule (2), namely:—

"(2) The Central Government may make rules defining for the purposes of this rule the principles to be followed in leaving out of account trading stock and stocks of raw materials."

DEFENCE OF INDIA RULES—R. 94-A (CONTROL OF CAPITAL ISSUES).

Notification No. 5-D. C. (27)/43 dated the 17th May 1943.

In exercise of the powers conferred by Section 2 of the Defence of India Act, 1939, the Central Government is pleased to direct that the following further amendment shall be made in the Defence of India Rules, namely:—

After Rule 94 of the said Rules, the following Rule shall be inserted, namely:—

"94-A. *Control of capital issues.*—(1) For the purposes of this Rule—

(a) securities shall include shares, stocks, bonds; debentures and debenture stocks, issued by or for the benefit of a company:

(b) a person shall be deemed to make an issue of capital who issues any securities whether in cash or otherwise.

(2) Subject to such exemptions as may be granted by order of the Central Government, no company, whether incorporated in British India or not, shall, except with the consent of the Central Government—

(a) make an issue of capital in British India ;

(b) make in British India any public offer of securities for sale ;

(c) renew or postpone the date of maturity or repayment of any security maturing for payment in British India.

(3) Subject to such exemptions as may be granted by order of the Central Government no company incorporated in British India shall, except with the consent of the Central Government make an issue of capital anywhere.

(4) Subject to such exemptions as may be granted by order of the Central Government, no person shall issue in British India any prospectus or other document offering for subscription or publicly offering for sale any security which does not include a statement that the consent of the Central Government has been obtained to the issue or offer of the securities.

(5) No person shall subscribe for any securities issued by a Company in respect of any issue of capital made in British India or elsewhere unless such issue has been made with the consent of the Central Government.

(6) If any person contravenes the provisions of this rule he shall be punishable with imprisonment for a term which may extend to five years or with fine or with both."

EXCESS PROFITS TAX RULES, 1940—DRAFT AMENDMENTS.

Notification No. 2 dated the 22nd May 1943.

The following draft of a further amendment to the Excess Profits Tax Rules, 1940, which the Central Board of Revenue proposes to make in exercise of the powers conferred by Section 27 of the Excess Profits Tax Act, 1940 (XV of 1940), is published for the information of all parties likely to be affected thereby, and notice is hereby given that the draft will be taken into consideration on or after the 2nd June 1943.

Any objection or suggestion which may be received from any person in respect of the said draft before the date specified will be taken into consideration by the Board.

To rule 20 of the said Rules the following proviso shall be added, namely :—

" Provided that, if, in relation to any chargeable accounting period, a company to which this rule applies gives notice to the Excess Profits Tax Officer, within the time allowed under Section 13 of the Act, for the furnishing of a return in respect of such chargeable accounting period, that the provisions of this Rule shall not be applied to it, its profits and average capital in relation to such chargeable accounting period shall be computed as if this Rule had not been made."

Notification No. 3 dated the 22nd May 1943.

The following draft of certain further amendments to the Excess Profits Tax Rules, 1940, which the Central Board of Revenue proposes to make in exercise of the powers conferred by Section 27 of the Excess Profits Tax Act, 1940 (XV of 1940), is published for the information of persons likely to be affected thereby and notice is hereby given that the draft will be taken into consideration on or after the 2nd June 1943.

Any objection or suggestion which may be received from any person in respect of the said draft before the date specified will be considered by the Board.

I. In the said Rules—

After Rule 6 the following rule shall be inserted, namely :—

“ 6A. Notice under sub-section (2) of Section 14A of the Act shall be in form E. P. 3-1 and the order of assessment and notice of demand in respect of professional assessments made under sub-section (3) of the said section shall be in form E. P. 4-7.”

II. In the Schedule annexed to the said Rules :—

(1) After Form E. P. 1 the following form shall be inserted namely :—

FORM E. P. 3-1.

EXCESS PROFITS TAX.

Notice under sub-section (2) of Section 14A of the Excess Profits Tax Act, 1940 (XV of 1940).

Excess Profits Tax Office.....

Dated the.....194 .

To

.....

Whereas a notice under sub-section (1) of Section 13 of the Excess Profits Tax Act, 1940 (XV of 1940), in respect of the chargeable accounting period commencing.....19... and ending.....19... has been served on you on.....19....
 I hereby give you notice of my intention to make a provisional assessment in accordance with the provisions of sub-section (3) of Section 14A of the said Act as follows :—

If you object to the amount of such proposed provisional assessment you should, within fourteen days of receipt of this notice, deliver to me a statement of your objections thereto.

Signed

Excess Profits Tax Officer.

(2) After Form E. P. 4 the following form shall be inserted namely :—

FORM E. P. 4-7.

EXCESS PROFITS TAX.

ASSESSMENT ORDER AND NOTICE OF DEMAND IN
RESPECT OF PROVISIONAL ASSESSMENTS MADE
UNDER SUB-SECTION (3) OF SECTION 14A OF THE
EXCESS PROFITS TAX ACT, 1940 (XV OF 1940).

To

.....
.....
.....

1. Take notice that, following the issue on the
19 , of notice under the sub-section (2) of Section 14A of the
Excess Profits Tax Act, 1940 (XV of 1940), of my intention to make a
provisional assessment in respect of your estimated liability to Excess
Profits Tax for the chargeable accounting period commencing 19
and ending 19 , I,* having
taken into account your statement of objection thereto dated
19 , have determined
provisionally the excess profits of such period to be the sum of
Rs. and that the Excess Profits Tax payable in respect
thereof is—

Rs.

| | | | |
|-------------------------------|----|-------|----------|
| for the period commencing | 19 | | |
| and ending | 19 | Rs. | @ 50%— |
| and for the period commencing | 19 | | |
| and ending | 19 | Rs. | @ 66⅔% - |
| | | Total | <hr/> |

2. You are required to pay the amount on or before.....

.....194... to
† Treasury Officer
Sub-Treasury Officer
Branch of Imperial Bank of India
Reserve Bank of India.

at when you will be granted a receipt.

3. If you do not pay the amount on or before

19 , you will be liable to a penalty
under Section 46 (1) of the Indian Income-tax Act, 1922, as applied to
Excess Profits Tax by Section 21 of the Excess Profits Tax Act, 1940
(XV of 1940), which may be as great as the amount of the Excess
Profits Tax hereby assessed.

* Delete inappropriate words.

INCOME-TAX ESTABLISHMENTS.*Notification No. 4 dated the 17th April 1943.*

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in its notification No. 19-Income-tax, dated the 1st April 1939, namely :—

In the said notification, after the preamble, the following proviso shall be inserted, namely :—

“Provided that nothing herein contained shall apply to cases or classes of cases assigned to a Commissioner of Income-tax appointed under sub-section (2) of Section 5 of the Indian Income-tax Act, 1922.”

Notification No. 5-D dated the 17th April 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in its notification No. 19 Income-tax, dated the 1st April 1939, namely :—

In the Schedule annexed to the said notification after Serial No. 51-A, the following entry shall be inserted, namely :—

| | | | | | |
|------|-------------------------------------------------|----------------------------------|-----------------------------------------------------------------------------------------|-----------------------------------------------------------------|-----|
| 51-B | Employees of the Govern- ment of Burma | Income-tax Officer, Simla. | Inspecting Assistant Commis- sioner of Income-tax, Amritsar Division. | Appellate Assistant Commis- sioner, Delhi Range. | do. |
|------|-------------------------------------------------|----------------------------------|-----------------------------------------------------------------------------------------|-----------------------------------------------------------------|-----|

Notification No. 5 dated the 1st May 1943.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that with effect from the 1st November 1942, the following further amendment shall be made in the Schedule appended to its Notification No. 58 Income-tax dated the 15th July 1939, namely :—

In the said Schedule, under the sub-head “I—Madras—” entry No. (9) against the Trichinopoly Range shall be omitted.

Notification No. 6 dated the 1st May 1943.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in its notification, No. 58-I.T. dated the 15th July 1939, namely :—

In the Schedule annexed to the said notification under the sub-head “II.—Bombay, Sind, British Baluchistan and Ajmer-Merwara” for entry No. (1) against “Bombay ‘A’”, the following entry shall be substituted, namely :—

“(1) All Sections of the Income-tax Department, (Central Bombay).”

Notification No. 6-D dated the 15th May 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in its notification No. 19-Income-tax dated the 1st April 1939, namely :—

In the Schedule annexed to the said notification, for Serial No. 38 the following shall be substituted, namely :—

| | | | | |
|------------------------------------------------|--------------------------------|---------------------------------------------------------------------------|-------------------------------------------------------------------------|--------------------------------------------------------------------------------|
| " 38 Employees of the Oudh and Tirhut Railway. | Income-tax Officer, Gorakhpur. | Inspecting Assistant Commissioner of Income-tax, Eastern Range, Cawnpore. | Appellate Assistant Commissioner of Income-tax, Lucknow Range, Lucknow. | Commissioner of Income-tax, United Provinces and Central Provinces and Berar." |
|------------------------------------------------|--------------------------------|---------------------------------------------------------------------------|-------------------------------------------------------------------------|--------------------------------------------------------------------------------|

Notification No. 7-D dated the 22nd May 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendments shall be made in its notification No. 19-Income-tax, dated the 1st April 1939, namely :—

In the Schedule annexed to the said notification—

(i) for the entry in column 6 against Serial Nos. 42 to 51-B, the following entry shall be substituted namely :—

" Commissioner of Income-tax, Punjab, N.W.F. and Delhi Provinces."

(ii) for the entry in column 4 against Serial No. 52, the following entry shall be substituted, namely :—

" Inspecting Assistant Commissioner of Income-tax, Southern Range, Bihar and Orissa."

Notification No. 8-D dated the 22nd May 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), as applied to the Hyderabad Administered Areas, the Central Board of Revenue directs that the following further amendment shall be made in its Notification No. 2-D.—Income-tax, dated the 2nd March 1940, namely :—

In the Schedule annexed to the said notification, for the entry in column 6 against Serial No. 5, the following entry shall be substituted, namely :—

" Commissioner of Income-tax, Punjab, N. W. F. and Delhi Provinces."

Notification Applying Indian Finance Act, 1943, to Br. Baluchistan.*Notification No. 52-F dated the 21st April 1943.*

In pursuance of sub-section (2) of Section 95 of the Government of India Act, 1935, the Governor-General in his discretion is pleased to direct that the Indian Finance Act, 1943 (VIII of 1943), shall apply to British Baluchistan.

Income Tax Reports.

VOLUME XI—PARTS XII & XIII.

DEFENCE OF INDIA RULES—RULE 94A.

Press Note.—A Press Note has been issued to remove certain doubts and misconceptions shown to exist by a month's experience of the working of the control of capital issues imposed by the Defence of India Rule 94A. The purport of the press note is as follows:—

'Company'.—The term "Company" is not qualified in any way in the Rule, which accordingly applies to issues of capital etc., made by any company, whether registered before or after the Rule came into effect (May 17, 1943) and whether public or private.

'Issue of capital'.—The term "issue of capital" used in the Rule refers to the completion of all processes by which the subscriber or lender comes into final possession of his security. In the case of shares, this process generally speaking is not completed until allotment is made and communicated to the subscriber: the making of an allotment or the issue of an allotment letter on or after May 17, 1943, therefore, requires the consent of Government. An exception is provided by the case of shares subscribed in the memorandum of association; it has been established by judicial decisions that the issue of such shares is completed with the registration of the memorandum.

Exemption to prevent delay in registration of companies.—In order not to delay dealings with the Registrars of Companies, the Government of India are now promulgating a general order exempting from the requirement of their consent the issue of shares for a consideration not exceeding Rs. 1,000 in all to the subscribers to a memorandum of association.

Procedure.—Specimen questionnaires are under active preparation, but applications will still have to be in the form of letters addressed to the Examiner of Capital Issues, Finance Department, Government of India, New Delhi. Meanwhile such letters must give particulars of the shares, debentures or other securities which the company proposes to issue or offer for sale, together with a statement of the objects which the company or its promoters have in view in respect of the particular issue or offer and of the amounts out of the capital or loan sought to be raised which it is proposed to devote to different headings of expenditure. The statement of objects should be much more precise than the very wide field usually covered by a memorandum of association.

EXCESS PROFITS TAX (POST-WAR REFUNDS) RULES, 1942—AMENDMENTS.

Notification No. 6 dated the 13th June 1943.

In exercise of the powers conferred by sub-section (3) of Section 10 of the Indian Finance Act, 1942 (XII of 1942), and Section 2 of the Excess Profits Tax Ordinance, 1943 (No. XVI of 1943), the Central Government is pleased to direct that the following further amend-

ments shall be made in the Excess Profits Tax (Post-war Refunds) Rules, 1942, namely :—

In the said Rules—

(1) in rule 2, after clause (iv) the following clause shall be inserted, namely :—

“(v) ‘Chargeable accounting period’ means chargeable accounting period as defined in sub-section (6) of Section 2 of the Act.”

(2) in rule 3, after the letters and figures “E. P. 4-1” the letters and figures, “E. P. 4-1A” shall be inserted.

(3) in rule 4—(i) in the first paragraph, after the letters and figures “E. P. 4-1” the words, letters and figures “in the case of chargeable accounting period ending not later than the 31st day of December 1942, and in form E. P. 4-1A in the case of a chargeable accounting period ending after that date,” shall be inserted ;

(ii) in the second paragraph, after the words “permitted thereby” the words and figures “or, in the case of a chargeable accounting period ending after the 31st day of December 1942, the amount required thereby”, shall be inserted.

(4) in rule 6, after the words “that may be”, the words “or is required to be” shall be inserted.

Form E. P. 4-1A.

EXCESS PROFITS TAX.

Notice under Section 2 of the Excess Profits Tax Ordinance, 1943, read with Section 10 of the Finance Act, 1942.

To

The amount of Excess Profits Tax payable by you at the rate of 66 $\frac{2}{3}$ per cent. in respect of the chargeable accounting period commencing.....194 and ending.....194 having been determined to be the sum of Rs. _____ as specified in the accompanying Notice of Demand given under Rule 5 of the Excess Profits Tax Rules and the date upon which such amount of Excess Profits Tax is made payable being the _____ day of _____ 194 ;

Take Notice that you are required under the provisions of Section 2 of the Excess Profits Tax Ordinance, 1943, read with Section 10 of the Finance Act, 1942, to deposit with the

* Treasury Officer

Sub-Treasury Officer

Agent, Imperial Bank of India

Governor, Reserve Bank of India

at

on or before the _____ day of

194 , the sum of Rs. _____

when you will be granted a receipt. A Chalan is enclosed for the purpose.

Excess Profits Tax Officer,
Address.

Dated

194 .

2. This Department Notification No. 4 Excess Profits Tax, dated the 5th June 1943 is hereby cancelled.

* Delete words that are inappropriate.

EXCESS PROFITS TAX RULES, 1940—AMENDMENTS.*Notification No. 5 dated the 12th June 1948.*

In exercise of the powers conferred by Section 27 of the Excess Profits Tax Act, 1940 (XV of 1940), the Central Board of Revenue directs that the following further amendments shall be made in the Excess Profits Tax Rules, 1940, the same having been previously published as required by sub-section (3) of the said section, namely :—

1. After rule 6 of the said Rules, the following rule shall be inserted, namely :—

“ 6A. Notice under sub-section (2) of Section 14A of the Act shall be in form E. P. 3-1 and the order of assessment and notice of demand in respect of provisional assessments made under sub-section (3) of the said section shall be in form E. P. 4-7 ”.

2. In the Forms set out in the Schedule annexed to the said Rules—

(1) after Form E. P. 1, the following Form shall be inserted, namely :—

Form E, P. 3-1.**EXCESS PROFITS TAX.**

Notice under sub-section (2) of Section 14A of the Excess Profits Tax Act, 1940 (XV of 1940).

Excess Profits Tax Office.

Dated the 194 .

To

Whereas a notice under sub-section (1) of Section 13 of the Excess Profits Tax Act, 1940 (XV of 1940), in respect of the chargeable accounting period commencing 19 and ending 19 has been served on you on 19, I hereby give you notice of my intention to make a provisional assessment in accordance with the provisions of sub-section (3) of Section 14A of the said Act as follows :—

If you object to the amount of such proposed provisional assessment you should, within fourteen days of receipt of this notice, deliver to me a statement of your objections thereto

Signed.

Excess Profits Tax Officer.”

(2) after Form E. P. 4, the following Form shall be inserted, namely :—

Form E. P. 4-7.**EXCESS PROFITS TAX.**

Assessment Order and notice of demand in respect of provisional assessments made under sub-section (3) of Section 14A of the Excess Profits Tax Act, 1940 (XV of 1940).

To

1. Take notice that, following the issue on the 19..... of notice under sub-section (2) of Section 14A of the Excess Profits Tax

Act, 1940 (XV of 1940) of my intention to make a provisional assessment in respect of your estimated liability to Excess Profits Tax for the chargeable accounting period commencing 19 and ending 19, I, having taken into account your statement of objections thereto dated 19, have determined provisionally the excess profits of such period to be the sum of Rs. and that the Excess Profits Tax payable in respect thereof is --

| | | | |
|-------------------------------|----|-----|---------|
| for the period commencing | 19 | Rs. | 19 |
| and ending | 19 | Rs. | 6 50/- |
| and for the period commencing | 19 | Rs. | 19 |
| and ending | 19 | Rs. | 66 33/- |
| Total | | | |

2. You are required to pay the amount on or before 19 to Treasury Officer
Sub-Treasury Officer
to Branch of Imperial Bank
of India
Reserve Bank of India

at when you will be granted a receipt.

3. If you do not pay the amount on or before 19, you will be liable to a penalty under Section 46 (1) of the Indian Income-tax Act, 1922, as applied to Excess Profits Tax by Section 21 of the Excess Profits Tax Act, 1940 (XV of 1940) which may be as great as the amount of the Excess Profits Tax hereby assessed.

Excess Profits Tax Officer.

Address.

Dated 19 .

* Delete inappropriate words.

INCOME TAX ESTABLISHMENTS.

Notification No. v-D dated the 12th June 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922, (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in its notification No. 19-Income-tax, dated the 1st April, 1939, namely:—

In the Schedule annexed to the said notification, after Serial No. 26, the following entry shall be inserted, namely:—

"26A Employees of the Bata Shoe do do do"
Company Limited stationed
any where in British India.

Notification Applying Excess Profits Tax Ordinance, 1943, to British Baluchistan.

Notification No. 22-W, dated the 27th May 1944.

In pursuance of sub-section (2) of section 95 of the Government of India Act, 1935, the Governor General in his discretion is pleased to direct that the Excess Profits Tax Ordinance, 1943 (Ordinance No. XVI of 1943), shall apply to British Baluchistan.

Income Tax Reports.

VOLUME XI—PARTS XIV & XV.

DEFENCE OF INDIA RULES, R. 94A—AMENDMENTS.

Notification No. 5-DC (27)/43 dated the 23rd June 1943.

In exercise of the powers conferred by Section 2 of the Defence of India Act, 1939 (XXXV of 1939), the Central Government is pleased to direct that the following further amendments shall be made in the Defence of India Rules, namely:—

In rule 94A of the said rules,—

(a) after sub-rule (2) the following sub-rule shall be inserted, namely:—

“(2A) The Central Government may qualify any consent accorded by it under sub-rule (2) with such conditions, whether for immediate or future fulfilment, as it may think fit to impose; and where a company acts in pursuance of such consent, it shall comply with the terms of any conditions so imposed.”

(b) after sub-rule (5) the following sub-rule shall be inserted namely:—

“(5A) No person shall purchase or sell any securities issued by a company in respect of any issue of capital made after the 17th May 1943 in British India or elsewhere, unless such issue has been made with the consent of the Central Government.”

*Notification No. D/558 EC 1/43 dated the 23rd June 1943
under R. 94-A (2), Defence of India Rules.*

In exercise of the power conferred by sub-rule (2) of the Defence of India Rule, 94A, the Central Government is pleased to exempt from the operation of that sub-rule the following transactions, namely:—

Issues of shares for a consideration not exceeding one thousand rupees in all to the subscribers of a memorandum of association.

Notification No. D/1319-EC1/43 dated the 9th July 1943.

In exercise of the power conferred by sub-rule (2) of Rule 94-A of the Defence of India Rules, the Central Government is pleased to direct that the following amendments shall be made in its notification in the Finance Department No. D/558 EC1/43, dated the 23rd June 1943, namely:—

I. The existing item beginning with the words “Issue of shares” shall be numbered as item (1);

II. after the item as so numbered the following shall be inserted as item (2), namely:—

(2) Issues of securities by persons in the ordinary course of their normal business and strictly and solely for the purposes of that business to a person carrying on the business of banking or his nominee in respect of advances made or to be made or overdrafts granted or to be granted by that person from time to time (not being advances made or to be made or overdrafts granted or to be granted on the terms express or implied that the advance or overdraft will or may be discharged wholly or partly by the issue of any securities or by the transfer of any

securities subsequently issued, or will or may be repaid wholly or partly out of the proceeds of any securities subsequently issued).

Indian Finance (Income-tax) Rules, 1942—Amendment.

Notification No. 12D dated the 17th July 1943.

In exercise of the powers conferred by sub-section (3) of Section 10 of the Indian Finance Act, 1942 (XII of 1942), the Central Government is pleased to direct that the following further amendment shall be made in the Indian Finance (Income-tax) Rules, 1942, namely :—

Rule 1 of the said Rules shall be renumbered as sub-rule (1) of that rule, and to that rule as so renumbered, the following sub-rule shall be added, namely :—

“(2) They apply to the whole of British India including British Baluchistan and those excluded and partially excluded areas to which the Indian Finance Act, 1942, has been or may hereafter be applied by notification under sub-section (1) of Section 92 of the Government of India Act, 1935.”

Indian Finance (Income-tax) Rules, 1943—Amendment.

Notification No. 14D Dated the 17th July 1943.

In exercise of the powers conferred by sub-sec. (9) of Section 5 of the Indian Finance Act, 1943 (VIII of 1943), the Central Government is pleased to direct that the following amendment shall be made in the Indian Finance (Income-tax) Rules, 1943, namely :—

Rule 1 of the said Rules shall be renumbered as sub-rule (1) of that rule, and to that rule as so renumbered, the following sub-rule shall be added, namely :—

“(2) They apply to the whole of British India including British Baluchistan and those excluded and partially excluded areas to which the Indian Finance Act, 1943, has been or may hereafter be applied by notification under sub-section (1) of Section 92 of the Government of India Act, 1935.”

Excess Profits Tax (Post-War Refunds) Rules, 1942—Amendment.

Notification No. 13D dated the 17th July 1943.

In exercise of the powers conferred by Section 10 of the Indian Finance Act, 1942 (XII of 1942), the Central Government is pleased to direct that the following further amendment shall be made in the Excess Profits Tax (Post-War Refunds) Rules, 1942, namely :—

Rule 1 of the said Rules shall be renumbered as sub-rule (1) of that rule, and to that rule as so renumbered, the following sub-rule shall be added, namely :—

“(2) They apply to the whole of British India including those excluded and partially excluded areas to which the Indian Finance Act, 1942, has been or may hereafter be applied by notification under sub-section (1) of Section 92 of the Government of India Act, 1935.”

Income-tax Establishments—

Notification No. 13 dated the 10th July 1943.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that

the following further amendments shall be made in the Schedule appended to its Notification No. 58-Income-tax, dated the 15th July 1939, namely :—

In the said Schedule under the sub-head "I-Madras"—

(i) After the existing entries against the Trichinopoly Range, the following entries shall be added, namely :—

"(13) Cuddalore.

(14) Negapatam.

(15) Tanjore."

(ii) Entries Nos. (21), (22) and (23) against the Madras Range shall be omitted.

Notification No. 10-D dated the 10th July 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in its notification No. 19-Income-tax, dated the 1st April 1939, namely :—

In the Schedule annexed to the said notification, for the entry in column 4 against Serial No. 62, the following entry shall be substituted, namely :—

"Inspecting Assistant Commissioner of Income-tax, Poona."

Income-tax Rules, 1922, R. 16—Amendments.

Notification No. 14 dated the 17th July 1943.

In exercise of the powers conferred by sub-section (1) of Section 59 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendments shall be made in the Indian Income-tax Rules, 1922, the same having been previously published as required by sub-section (4) of the said section namely :—In the said Rules—

(1) in rule 16, for the figure "1,600" the figure "1,200" shall be substituted :

(2) in the verification appended to the Form set forth in rule 17—

(i) for the figure "1,600", in both places where it occurs the figure "1,200" shall be substituted ;

(ii) after the words "to all persons" the following words, figures and brackets shall be inserted, namely :—

"(except those in respect of whom a separate ^{statement} _{return} required by rule ¹⁴/₁₅ of the Indian Finance (Income-tax) Rules, 1942, read with the Indian Finance (Income-tax) Rules, 1943, has been made)."

Control of Capital Issues—Press Note of July 10.

A Press Note to the following effect has been issued on the 10th July 1943—

In their recent Press Note dated June 21, 1943, the Government of India clarified certain technical points relating to the control of capital issues. Since apprehension continues to be expressed in certain quarters as to the fundamental principles involved in this control the

Government of India desire to draw the attention of the public to the following points :

At the present time there is the most serious shortage of many of the most essential goods and services, including not only iron and steel, machines and mill stores, but also of skilled labour and of transport facilities. These shortages grow directly out of the war situation, and cannot be wholly remedied so long as the war lasts.

In order to prevent a scramble for the available supplies, which can only result in raising prices still further, it appears best to encourage those industrialists whose enterprises will directly assist in aiding the war effort or will be in a position to embark upon production of essential consumers' goods at an early date. There is no public purpose in allowing priority to the manufacture of luxury goods, for instance, when the same capital equipment can go to the production of articles in more common use. Without control of capital issues, there is no guarantee that such supplies as are available will in fact go to the most suitable applicant.

Control thus serves in present conditions to further industrialisation on sound lines. These remarks apply with even more force when the contemplated enterprise purports to be in a position to produce only at the end of the war. Such enterprises may also compete for plant, skilled labour etc., and they can certainly add nothing to immediate productivity. A special care is, therefore, required in dealing with them.

Consent will, however, be granted in suitable cases for an issue of capital required to purchase plant or machinery for which an order has been placed for delivery after the war, subject to the condition that the money is invested in defence loans or other new Government securities and is kept so invested until it can be spent for the intended purpose.

Moreover, in so far as the so-called new undertakings merely take the form of offering to the public shares in enterprises which were already in existence, but which have been converted to a joint stock basis (sometimes at extremely inflated prices), no net addition to the productive resources of the country is made at all, and the only effect is to swell the speculative boom which is already assuming an unhealthy form, and possibly to secure advantages in the matter of taxation at the expense of the general tax-payer.

Secondly, it will be generally agreed that the battle against inflationary tendencies cannot be won unless there is a large scale subscription to the various loans issued by the Government of India. Although part of the capital subscribed to new banks, investment trusts and insurance companies will no doubt flow into these loans, Government have to consider whether there is not a danger that a good deal of it may be diverted to speculative uses, such as the financing or hoarding of scarce commodities and loans to the stock exchange which are definitely anti-social at the present time.

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DEFENCE OF INDIA RULES, R. 94-A—AMENDMENTS.

Notification No. 5-DC (27)/43 dated the 2nd August 1943.

In exercise of the powers conferred by Section 2 of the Defence of India Act, 1939 (XXXV of 1939), the Central Government is pleased to direct that the following further amendments shall be made in the Defence of India Rules, namely:—

In rule 94A of the said Rules,—

(a) after sub-rule (4) the following sub-rule shall be inserted, namely:—

“(4A) The Central Government may by order condone a contravention of sub-rule (2), sub-rule (3) or sub-rule (4), and on the making of such order the provisions of this rule shall have effect as if an exemption had been granted under sub-rule (2), sub-rule (3) or sub-rule (4), as the case may be, in favour of the thing done in contravention of such sub-rule.”

(b) at the end of sub-rule (5A) the following shall be added, namely:—

“or unless the security concerned is one which, having before the 23rd June 1943 been the subject of a transaction which would have been prohibited if it had been effected on or after that date, is endorsed with a Certificate by the Examiner of Capital Issues or an officer authorised by him in this behalf that it has on this ground been exempted by the Central Government from the operation of this sub-rule.”

Excess Profits Tax Rules, 1940—Amendment.

Notification No. 7 dated the 24th July 1943.

In exercise of the powers conferred by Section 27 of the Excess Profits Tax Act, 1940 (XV of 1940), the Central Board of Revenue directs that the following further amendment shall be made in the Excess Profits Tax Rules, 1940, the same having been previously published as required by sub-section (3) of the said section, namely:—

To rule 20 of the said Rules the following proviso shall be added, namely:—

“Provided that, if, in relation to any chargeable accounting period, a company to which this rule applies gives notice to the Excess Profits Tax Officer, within the time allowed under Section 13 of the Act, for the furnishing of a return in respect of such chargeable accounting period, that the provisions of this Rule shall not be applied to it, its profits and average capital in relation to such chargeable accounting period shall be computed as if this Rule had not been made.”

Excess Profits Tax (Post-War Refunds) Rules, 1942—Amendments.*Notification No. I-C dated the 7th August 1943.*

In exercise of the powers conferred by sub-section (3) of Section 10 of the Indian Finance Act, 1942 (XII of 1942), and that sub-section read with sub-section (5) of Section 2 of the Excess Profits Tax Ordinance, 1943 (No. XVI of 1943), the Central Government is pleased to direct that the following further amendments shall be made in the Excess Profits Tax (Post-War Refunds) Rules, 1942, namely :—

In the said Rules—

(1) in rule 2, after clause (v) the following clause shall be inserted, namely :—

“(vi) “the Ordinance” means the Excess Profits Tax Ordinance, 1943 (No. XVI of 1943).”;

(2) for rule 3, the following rule shall be substituted, namely :—

“3 (1). The Excess Profits Tax Officer shall give notice of the provisions of Section 10 of the Finance Act to each person who has been or may hereafter be assessed to excess profits tax at 66 $\frac{2}{3}$ per cent. for any chargeable accounting period ending not later than the 31st day of December 1942. Such notice shall be in Form E. P. 4-1 but in any case in which, when the Finance Act came into operation, excess profits tax notices of demand had already been issued, the notice shall be in Form E.P. 4-2.

(2) The notice required to be given under Section 2 of the Ordinance shall be in Form E. P. 4-1A.

(3) Notices in Form E.P. 4-1 shall be given at the time of issue of any notice of demand in respect of excess profits tax under Section 14 of the Act but notices in Form E. P. 4-2 shall be given forthwith.”;

(3) in rule 4—

(i) the first paragraph of the rule shall be omitted;

(ii) in the second paragraph for the words “permitted thereby, the amount of the excess shall be refunded” the following shall be substituted, namely :—

“permitted thereby, or the deposit made under Section 2 of the Ordinance exceeds the amount required thereby, the amount of the excess shall be refunded with interest at 2 per cent. per annum from the date of deposit to the date of repayment.”;

(4) in rule 5, after the words “the Finance Act” the words “or under Section 2 of the Ordinance” shall be inserted;

(5) in rule 6, after the words “the Finance Act” the words “or under Section 2 of the Ordinance” shall be inserted.

Auditor's Certificates Rules—Amendment.*Notification No. I-A (3)/48 dated the 24th July, 1948.*

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section namely :—

In the proviso to rule 18 of the said Rules, the words “and copies of the same placed on sale” shall be omitted.

Income Tax Reports.

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Auditor's Certificates Rules, 1932—Amendment.

Notification No. 1-A (4)/43 dated the 21st August 1943.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely:—

In rule 16 of the said Rules, to sub-rule (1) the following words shall be added, namely:—

“provided that if the Central Government is satisfied that the annual fee was not paid by reason only of the transfer of the name of a person from the Indian Register to the Burma Register of Accountants, arrears on account of the annual fee shall not be required to be paid, and if paid may be refunded.”

Income-tax Rules, 1922—(R. 13) Amendment.

Notification No. 15 dated the 14th August 1943.

In exercise of the powers conferred by sub-section (1) of Section 59 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in the Indian Income-tax Rules, 1922, the same having been previously published as required by sub-section (4) of the said section, namely :—

For the form prescribed in Rule 13 of the said Rules, the following form shall be substituted, namely:—

" Certificate of deduction of income-tax from the interest

bearer bonds

ON _____
promissory notes/stock certificate/Subsidiary General Ledger Account Balance
Dividend No. of coupon
Draft No.

* Number of receipt for interest.

* (This number should also appear in the interest pages on the back of the Government promissory notes).

Certified that Rupees.....being income-tax at the rate of.....pies per Rupee has been deducted from the interest coupons for Rs.....presented for payment by the draft in the interest receipt of this date; from Rupees.....being the amount of interest on bearer bonds Government promissory notes/stock certificate/Subsidiary General Ledger Account Balance for Rs.....of the.....per cent. loan of..... said to be the property of standing in the name of

(Name of the office paying }
interest }
The 19 . }

Signature
(Designation of the official
paying interest.)

To be signed by the claimant.

I hereby declare that the bearer bonds Government Promissory notes/stock certificates /Subsidiary General Ledger Account Balance on which interest, as above specified, has been received were my own property and were in the possession of.....at the time when income-tax was deducted.

Signature

Date.

N.B.—1. The inappropriate words to be struck out.

2. The securities, or in the case of a Subsidiary General Ledger Account Balance, a certificate from the Public Debt Office or Office of the Reserve Bank of India concerned, to be produced when required, in support of any claim.

Note.—This certificate should not be returned to the Public Debt Office. In case you desire to claim a refund of the whole or any part of the tax deducted, as shown above, on the ground that your total annual income is below the taxable limit or is less than that to which the maximum rate of income-tax applied you should send this certificate to the Income-tax Office direct with an application in the prescribed form obtainable from that office."

Income-tax Establishment.

Notification No. 16 dated the 14th August 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendments shall be made in its notification No. 19-Income-tax, dated the 1st April, 1939, namely :—

In the Schedule annexed to the said notification, for Serial Nos. 4, 5, 7, 8, 9, 11 to 17, 17A and 18 the following shall be substituted, namely :—

| Serial No. | Persons. | Officers appointed to perform the functions of | | | |
|------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------|------------------------------------------------------------------------|-------------------------------------------------------------------------|---------------------------------------------------------------------------|
| | | Income-tax Officer. | Inspecting Assistant Commissioner of Income-tax. | Appellate Assistant Commissioner of Income-tax. | Commissioner of Income-tax. |
| 1 | 2 | 3 | 4 | 5 | 6 |
| 4 | Indian employees in Sind, Punjab and Delhi of Messrs. Ralli Brothers. | Income-tax Officer, Salaries, Karachi. | Inspecting Assistant Commissioner of Income-tax, Karachi Range. | Appellate Assistant Commissioner of Income-tax, Karachi Range. | Commissioner of Income-tax, Bombay, Sind and British Baluchistan, Bombay. |
| 5 | European staff of Messrs. Volkart Brothers working in the Punjab and Sind. | Ditto | Ditto | Ditto | Ditto |
| 7 | Military employees under the audit of the Controller of Military Accounts, Poona, and Southern Army, Poona. | Income-tax Officer, Salaries and Poona District, Poona. | Inspecting Assistant Commissioner of Income-tax, Belgaum Range, Poona. | Appellate Assistant Commissioner of Income-tax, Belgaum Range, Belgaum. | Ditto |
| 8 | Persons (excluding those who fall under S No. 62) not resident in British India whose total income is made up of income wholly taxed at source or dividends or both. | Income-tax Officer, Non-residents' Refund Circle, Bombay. | Inspecting Assistant Commissioner of Income-tax, B-Range, Bombay City. | Appellate Assistant Commissioner of Income-tax, A-Range, Bombay City. | Ditto |
| 9 | Persons (excluding those who fall under S. No. 62) not resident in British India and not assessed through statutory agents under Section 43 any part of whose income is derived from horse racing. | Income-tax Officer, Poona. | Inspecting Assistant Commissioner of Income-tax, Belgaum Range, Poona. | Appellate Assistant Commissioner of Income-tax, Belgaum Range, Belgaum. | Ditto |
| 11 | Pensioners who draw their pensions in the United Kingdom and reside in Indian States. | Income-tax Officer, Non-residents' Refund Circle, Bombay. | Inspecting Assistant Commissioner of Income-tax, B-Range, Bombay City. | Appellate Assistant Commissioner of Income-tax, Bombay City. | Ditto |
| 12 | Pensioners who draw their pensions through Post Offices in Indian States and reside in those States. | Ditto | Ditto | Ditto | Ditto |

| Serial No. | Persons. | Officers appointed to perform the functions of | | | |
|------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------|------------------------------------------------------------------------|-----------------------------------------------------------------------|---------------------------------------------------------------------------|
| | | Income-tax Officer. 3 | Inspecting Assistant Commissioner of Income-tax. 4 | Appellate Assistant Commissioner of Income-tax. 5 | Commissioner of Income-tax. 6 |
| 1 | 2 | | | | |
| 13 | Religious and charitable institutions outside British India not liable to Income-tax under Section 4 (3) (i) and (ii) of the Indian Income-tax Act applying for refund of tax deducted at source on interest on securities or for exemption certificates in respect thereof. | Income-tax Officer, Non-residents Refund Circle, Bombay. | Inspecting Assistant Commissioner of Income-tax, B-Range, Bombay City. | Appellate Assistant Commissioner of Income-tax, A-Range, Bombay City. | Commissioner of Income-tax, Bombay, Sind and British Baluchistan, Bombay. |
| 14 | "Thana Funds" administered by Political Agents in Kathiawar. | Ditto | Ditto | Ditto | Ditto |
| 15 | Local or Thana Funds administered by Government officers in Indian States or in British administered areas in those States which are either not liable to income-tax or have been exempted under Section 60 of the Act, when application is made on their behalf for refund of tax deducted at source on interest on securities or for exemption certificates in respect thereof. | Ditto | Ditto | Ditto | Ditto |
| 16 | All persons assessed under Section 44-C. | Ditto | Ditto | Ditto | Ditto |
| 17 | Employees of the Bombay-Baroda and Central India Railway and the Great Indian Peninsula Railway except those under the audit of the Audit Officer, Railway Collieries, Calcutta Government servants employed under the Director General of Observatories, Poona, the Director, Madras and Kodaikanal Observatories, the Meteorologist, Upper Air Observations, Agra, and the Meteorologist, Karachi, who are under the audit of the Accountant General, Bombay. | Income-tax Officer, Salaries, Section I, Bombay. | Ditto | Appellate Assistant Commissioner of Income-tax, B-Range, Bombay City. | Ditto |
| 17A | | Ditto | Ditto | Ditto | Ditto |
| 18 | Employees of the Rajputana Minerals Company, Limited. | Income-tax Officer, Salaries, Section II, Bombay. | Ditto | Ditto | Ditto |

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APPELLATE TRIBUNAL RULES—AMENDMENTS.

(23rd July 1943.)

In exercise of the powers conferred by sub-section (8) of Section 5A of the Indian Income-tax Act, 1922, the Appellate Tribunal hereby makes the following further amendments in the Appellate Tribunal Rules :—

1. In rule 8 for the words "New Delhi" the word "Bombay" shall be substituted.

2. For sub-rule (1) of rule 9, the following shall be substituted :—

"Each Bench shall have its headquarters at such place and hold sittings at such place or places as the President may direct and shall hear and determine such appeals as are assigned to it by the President by a general or special order."

3. Rule 11 shall be omitted.

4. For rule 12 the following shall be substituted :—

"The officers of the Tribunal shall observe the same office hours and holidays, other than vacations, as are observed by the Civil Court of the highest jurisdiction at the headquarters of the respective Benches except as otherwise ordered by the President or Benches concerned."

5. Rule 13 shall be omitted.

6. In rule 14 for the words "New Delhi" the word "Bombay" shall be substituted.

7. In rule 19 for the words "a copy," the words "two copies" shall be substituted.

8. In rule 29—(a) the words "after obtaining the records of the Income-tax Officer and the Appellate Assistant Commissioner" shall be omitted and ; (b) for the words "The notice to the respondent shall be accompanied by a copy of the grounds of appeal," the following shall be substituted :—"A copy of the grounds of appeal shall be sent to the respondent either with such notice, or before it."

9. For rule 36, the following shall be substituted :—

"36. (1) Where on the day fixed for hearing, or any other day to which the hearing may be adjourned, the appellant does not appear when the appeal is called on for hearing, the appeal, unless adjourned to some other day, may notwithstanding such default be decided on merits.

(2) Save with the permission of the Bench no appeal shall be withdrawn and when such permission has been granted the appeal shall be dismissed."

10. Rule 39 shall be omitted.

11. Rule 43 shall be omitted.

12. For rule 48, the following shall be substituted :—

"48. The application shall comply with the following :—

(a) The findings of fact arrived at in the order under sub-section (4) of Section 33 and relevant to the questions of law required to be referred to the High Court shall be stated therein.

(b) Each such question shall be concisely formulated therein.

(c) A list of documents giving particulars thereof which the applicant desires to be forwarded to the High Court shall be appended to it,"

13. In rule 49—

(a) after the words "findings of fact" the words "arrived at in the order under sub-section (4) of Section 33", shall be inserted, and

(b) the words "and allege what, but for that error of law, the findings ought to have been", shall be omitted.

14. For rule 50, the following shall be substituted :—

"Where the application is in order, it shall be registered in the Register of Reference Applications and sent with the relevant record for disposal to the Bench which decided the appeal or to such other Bench as the President may direct."

15. In rule 52 for the words "appellate order", the words "order under sub-section (4) of Section 33 or if no question of law has been formulated in the application" shall be substituted.

16. In rule 53 after the word "respondent", the words "accompanied by a copy of such application" shall be inserted.

17. In rule 54—

(a) for the words "appellate order" where they first occur, the words "order under sub-section (4) of Section 33" shall be substituted ;

(b) for the words "appellate order" where they occur for the second time the words "said order" shall be substituted ; and

(c) the following shall be added at the end :—

"A list of documents giving full particulars thereof which the respondent desires to be forwarded to the High Court shall be appended to the reply."

18. Rule 55 shall be omitted.

19. Rule 56 shall be omitted.

20. Rule 57 shall be omitted.

21. Rule 58 shall be omitted.

22. For rule 59, the following shall be substituted :—

"59. After giving the parties an opportunity to be heard the Bench shall dismiss the application if no question for reference to the High Court has been formulated in the application, or when it is of opinion that the question formulated by the applicant is not one of law or does not arise from the order under sub-section (4) of Section 33."

23. After rule 59, the following new rule shall be added :—

"59-A. Where the Bench considers that a question of law arises out of the order under sub-section (4) of Section 33, it shall draw up a statement of the case and send it together with the records to the Headquarters of the Tribunal."

24. Rule 60 shall be omitted.

25. Rule 61 shall be omitted.

26. Rule 62 shall be omitted.

27. In rule 63 the word "particular" shall be omitted.

28. Rule 64 shall be omitted.

29. In rule 68 the words "in the presence of the parties or after notice to them" shall be omitted.

30. After rule 70, the following new rule shall be added :—

"71. Application to the Tribunal for the inspection of documents or for the grant of certified copies of documents shall be in the forms prescribed by the President."

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EXCESS PROFITS DOUBLE TAXATION (INDIA AND COCHIN) RULES.

Notification No. 9 dated the 27th November 1943.

In exercise of the powers conferred by sub-section (1) of Section 11 of the Excess Profits Tax Act, 1940 (XV of 1940), the Central Government is pleased to make the following rules for the granting of relief in cases where, in respect of any profits of any business, excess profits tax has been paid under that Act and excess profits tax has also been paid in Cochin :—

1. These rules may be cited as the Excess Profits Double Taxation (India and Cochin) Rules.

2. In these Rules, the expression—

(i) “Indian excess profits tax” means any excess profits tax payable in accordance with the provisions of the Excess Profits Tax Act, 1940;

(ii) “Cochin excess profits tax” means any excess profits tax payable under the law in force in Cochin;

(iii) “Chargeable accounting period” has in British India the meaning assigned to it in sub-section (6) of Section 2 of the Excess Profits Tax Act, 1940, and in Cochin the meaning assigned to it in clause (4) of Section 2 of the Excess Profits Tax Act (II of 1117).

3. Any reference in these Rules to the lower of the two rates shall, where the rates are equal, be construed as a reference to either of those rates.

4. These Rules shall have effect in respect of Indian excess profits tax charged for any chargeable accounting period in respect of which under the law in force in Cochin relief is to be given in respect of the payment of Indian excess profits tax.

5. If the person carrying on a business in any chargeable accounting period proves to the satisfaction of the Excess Profits Tax Officer that he has paid in respect of any profits of the business in that period, Indian excess profits tax and that he has also paid, in respect of those profits, Cochin excess profits tax—

(i) there shall be computed the amounts of excess profits tax which would be payable in British India and Cochin respectively, if excess profits tax in the other country were disregarded except in computing capital;

(ii) the amount of relief to be given in British India shall be the same proportion of the lesser of the amounts so computed as the amount so computed for British India bears to the sum of the two amounts so computed;

(iii) if the amount so computed either for British India or for Cochin is found to have been incorrect (whether by reason of a subsequent deficiency of profits or for any other reason), the amount so computed shall be recalculated and the relief in British India revised accordingly.

6. Where the chargeable accounting periods differ in British India and Cochin the tax chargeable for such periods shall be apportioned on

a time basis to co-terminous periods as hereinafter defined, and relief shall be allowed under these rules for these periods.

For this purpose, except so far as the Government of India and the Government of Cochin otherwise agree—

(a) the first of the co-terminous periods shall commence on the first day on which double taxation commenced, and, each succeeding co-terminous period shall commence at the expiration of the period immediately preceding; and

(b) each of such co-terminous periods shall end at the end of the chargeable accounting period within which it commences, and, if the chargeable accounting periods differ for the purposes of the excess profits tax of the two countries, then at the end of that one of the chargeable accounting periods that ends first.

7. For the purposes of these Rules the liability to excess profits tax of a principal company of a group of inter-connected companies shall be taken to be the liability of that company in respect of its own business only.

Where, however, excess profits tax payable in respect of the business carried on by a subsidiary company is assessed on the principal company, relief shall be allowed to the subsidiary company as if the excess profits tax liability attributable to the business of the subsidiary company were separately assessed upon that company.

8. Every application for a refund of excess profits tax under these rules shall be made to the Excess Profits Tax Officer of the district or circle in which the applicant is chargeable to excess profits tax. Such application may be presented by the applicant in person or by a duly authorised agent or may be sent by post, and shall be in the form prescribed in rule 15 of the Excess Profits Tax Rules, 1940.

EXCESS PROFITS TAX (COMPUTATION OF PROFITS AND CAPITAL) RULES, 1943 (DRAFT).

Notification No. 10 dated the 27th November 1943.

The following draft of certain rules which the Central Government proposes to make in exercise of the powers conferred by sub-rule (3) of Rule 12 of Schedule I and sub-rule (2) of Rule 3 of Schedule II of the Excess Profits Tax Act, 1940 (XV of 1940) is published for the information of persons likely to be affected thereby and notice is hereby given that the draft will be taken into consideration on or after the 10th January 1944.

Any objection or suggestion which may be received from any person in respect of the said draft before the date specified will be considered by the Central Government.

Draft Rules.

1. (1) These Rules may be cited as the Excess Profits Tax (computation of profits and capital) Rules, 1943.

(2) They apply to the whole of British India and to the Excluded and Partially Excluded Areas to which the Excess Profits Tax Act, 1940 (XV of 1940) has been or may hereafter be applied.

2. In these Rules—

(i) "the Act" means the Excess Profits Tax Act, 1940 (XV of 1940);

(ii) "bonus" means any remuneration payable to any employee other than wages salary or commission;

(iii) "dearness allowance" means any bonus payable to any employee to compensate for the increased cost of living;

(iv) "manual wage-earner" means any wage-earner employed by way of manual labour and does not apply to any persons employed as clerks, typists, draftsmen or in any similar capacity;

(v) "wages" means any remuneration payable to a manual wage-earner except by way of dearness allowance or bonus;

(vi) "cost of living" means, in relation to any period, the proportionate cost, in relation to a common base as shown for that period by the Cost of living Index published by the Provincial Government and appropriate to the area in which the manual wage-earner resides.

3. In applying the provisions of Rule 12 of Schedule I of the Act to the computation of the profits of any chargeable accounting period—the sum to be allowed in respect of any bonus paid after the 30th November 1943 to any manual wage-earner, other than a dearness allowance, shall not exceed the sum of one quarter of the wages for the period in respect of which the bonus is paid.

4. In applying the provisions of Rule 12 of Schedule I of the Act to the computation of the profits of any chargeable accounting period—the sum to be allowed in respect of any dearness allowance paid to any employee after the 30th November 1943 shall not exceed—

(i) in the case where the salary or wages, in respect of which the dearness allowance is paid, are paid at the rate of Rupees 25 per month such a sum as, added to the amount of the salary or wages, bears to the amount of the salary or wages the same proportion as the cost of living for the period in respect of which such salary or wages are paid bears to the cost of living for the year ended 31st December 1939;

(ii) in the case where the salary or wages, in respect of which the dearness allowance is paid, are paid at the rate of less than Rupees 25 per month the sum that would be allowable if such salary or wages were paid at the rate of Rupees 25 per month;

(iii) in the case where the salary or wages, in respect of which the dearness allowance is paid, are paid at a rate exceeding Rupees 25 but not exceeding Rupees 60 per month

(a) the sum that would have been appropriate if the salary or wages had been paid at the rate of Rupees 25 per month only, plus

(b) in respect of such part of the salary or wages as represents payment at the rate of more than Rupees 25 per month three-quarters of the sum that would be allowed if such part had represented salary or wages paid at the rate of Rupees 25 per month;

(iv) in the case where the salary or wages, in respect of which the dearness allowance is paid, are paid at a rate exceeding Rupees 60 per month—

such part of the dearness allowance that would be allowed in the case of salary or wages paid at the rate of Rupees 60 per month as, added to the amount of the salary or wages, will not give a total which exceeds the rate of Rupees 300 per month.

Provided that where the employer provides food or other essential articles of consumption for an employee at rates less than the retail rates current in the locality in which the employee resides the cash value of such provision as estimated by the Excess Profits Tax Officer shall be treated as a dearness allowance.

5. In relation to chargeable accounting periods commencing after the 31st December 1942, payments in respect of bonuses and commission, exclusive of dearness allowances, payable to persons other than manual wage-earners and persons carrying on business within the definition of sub section (5) of Section 2 of the Act, shall be deemed to be unreasonable and unnecessary if and to the extent to which they exceed—

(i) in the case of a business the standard profits of which are computed by reference to the profits of a standard period,

(a) twice the sum that bears to the amount of such payments in the standard period the same proportion that the length of the chargeable accounting period bears to the length of the standard period, or

(b) one per cent. of the amount of the profits of the chargeable accounting period as computed for the purpose of assessment to excess profits tax, whichever is the greater ;

(ii) in the case of any other business, one per cent. of the amount of the profits of the chargeable accounting period as computed for the purposes of assessment to excess profits tax.

6. In applying the provisions of Rule 3 of Schedule II of the Act, in respect of trading stocks or stocks of raw materials, as the case may be, to the computation of the average capital during any chargeable accounting period commencing after the 31st December 1942—

there shall be ascertained by the Excess Profits Tax Officer the sum that bears to the sales of the business during such period the same proportion as the average amount of capital represented by such stocks during the standard period, if any, bears to the sales of the business during the standard period, and the excess, if any, of the average capital so represented during the chargeable accounting period over that sum shall be left out of account.

Provided that in the case of a business in which there is no standard period the sum to be left out of account shall be computed by reference to the proportion borne by such stocks to total sales in the case of similar businesses during their standard periods.

Provided further that no sum shall be left out of account under this Rule without the previous approval of the Inspecting Assistant Commissioner.

Provided further that where the Inspecting Assistant Commissioner is satisfied that the whole or any part of the excess was, owing to special circumstances, necessarily held for the requirements of the business the sum to be left out of account shall be correspondingly reduced.

Income-tax Establishments.

Notification No. 15-D dated the 16th October 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income Tax Act, 1922 (XI of 1922), the Central Board

of Revenue directs that the following further amendment shall be made in its notification No. 19—Income-tax, dated the 1st April, 1939, namely :—

In the Schedule annexed to the said notification, for Serial No. 51-B, the following shall be substituted, namely :—

| | | | | |
|--------|----------------------------------------------------------------------------------------------|---------------------------------------|---------------------------------------------------------------------|--------------------------------------------------------------|
| " 51-B | Employees of the Government of Burma working in the office of the Accountant General, Burma. | Income Tax Officer, Simla. | Inspecting Assistant Commissioner of Income Tax, Amritsar Division. | Appellate Assistant Commissioner of Income Tax, Delhi Range. |
| 51-C | Employees of the Government of Burma excluding those who fall under Serial No. 51-B. | Additional Income-tax Officer, Simla. | Do. | Do. |

Notification No. 18-D dated the 27th November, 1943.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act 1922, (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in its notification No. 19—Income-tax, dated the 1st April 1939, namely :—

In the Schedule annexed to the said notification, for Serial Nos. 51-B and 51-C, the following shall be substituted, namely :—

| | | | | | |
|---------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------|---------------------------------------------------------------------|--------------------------------------------------------------|-----|
| " 51-B. | All Civil (Gazetted employees of the Government of Burma under the audit of the Accountant General, Burma, and all Gazetted and non-Gazetted employees of the Posts and Telegraphs Department, Burma under the audit of the Comptroller of Posts and Telegraphs Accounts, Burma. | Income-tax Officer, Simla. | Inspecting Assistant Commissioner of Income-tax, Amritsar Division. | Appellate Assistant Commissioner of Income-tax, Delhi Range. | Do. |
| " 51-C. | Employees of the Government of Burma, excluding those who fall under Serial No. 51-B, and all Burma evacuees at Simla, excluding those who are covered by any of the other items in this Schedule. | Additional Income-tax Officer, Simla. | Do. | Do. | Do. |

Notification No. 17-D dated the 6th November, 1943.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), as applied to the Gwalior Residency Area,

the Central Board of Revenue directs that the Appellate Assistant Commissioner of Income-tax for the said Area shall perform his functions in respect of all persons and incomes assessed to income-tax and super-tax in the said Area.

Auditor's Certificates Rules, 1932—Amendments to.

Notification No. I-A (7)/43 dated the 18th September, 1943.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

In rule 19 of the said Rules, for the existing Proviso the following shall be substituted, namely :—

“ Provided that in respect of service rendered under articles for, and examinations passed of, any of the Institutes or Societies of Chartered Accountants in England and Wales, Scotland, or Ireland, or the Society of Incorporated Accountants and Auditors, London, the following concessions shall be admissible during the period of the war and for six months thereafter.

(a) Any period served under articles for the aforesaid Institutes and Societies will be set off against the practical training prescribed under rule 36.

(b) The passing of the Intermediate and Final Examinations of any of the aforesaid Institutes or Societies will be held as equivalent to the passing of the First and the Final Examinations, respectively, held under these Rules.”

Notification No. I-A (5)/43, dated the 16th October, 1943.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act 1913, (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

In rule 45 of the said Rules, for the words “ shall not be retained ” the following shall be substituted namely :—

“ shall not, except with the permission of the Central Government, be retained.”

Notification No. I-A (10)/43 dated the 13th November, 1943.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

In clause (a) of sub-rule (1) of rule 40 of the said Rules, after the word “ London ” the following shall be inserted, namely :—

“ but exclusive of articled clerks whose employment by the Registered Accountant under the said Bye-laws commenced before the 25th October 1941.”

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INDIAN INCOME-TAX RULES, 1922—AMENDMENT.

Notification No. 20 dated the 4th December 1943.

In exercise of the powers conferred by sub-section (1) of Section 59 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in the Indian Income-tax Rules, 1922, the same having been previously published as required by sub-section (4) of the said section, namely:—

After rule 11 of the said Rules, the following rule shall be inserted namely:—

“11-A. In the case of income chargeable under the head “Salaries” where deduction is not made by or on behalf of Government, the Commissioner of Income-tax may, in his discretion, notwithstanding anything contained in rule 10 and sub-rule (1) of rule 11, permit an employer to pay income-tax and super-tax on the income of his employees chargeable under the head “Salaries” in a lump sum every month based on the average amount of income-tax and super-tax deductible every month from such income and to submit at the end of the year to the Income-tax Officer within whose jurisdiction the deduction is made (or where there is more than one Income-tax Officer having jurisdiction in the same area to the Income-tax Officer specified by the Commissioner of Income-tax) a statement giving the following particulars:—

1. Name of employee.
2. Amount of salary (or wages) paid during the year.
3. Leave salary or allowance, if any, paid outside British India.
4. Period for which the salary (or wages) was paid.
5. House rent allowance paid during the year.
6. Value of rent-free quarters for the year.
7. Bonus, gratuity, fees, commissions, perquisites or other allowances, profits in lieu of or in addition to salary, payments made at or in connection with the termination of employment, advances of salary, etc., and all other sums paid which are chargeable to income-tax. (Full details showing the total amount paid during the year, periods for which the payments were made are to be given separately for each item.)
8. Salary, bonus and all other sums which were due to be paid during the year but which were not actually paid. (Full details showing the amount, the due date, and the period for which the amount was payable are to be given for each item separately).

9. Total of items 2, 3, 5, 6, 7 and 8 above.

10. Yearly amounts paid or deducted in respect of provident or superannuation or other funds and life insurance premiums (give details).

11. Net amount upon which tax has been deducted during the year.

12. Total amount of income-tax deducted during the year (surcharge to be shown separately).

13. Total amount of super-tax deducted during the year (surcharge to be shown separately).

Such permission which will hold good till it is withdrawn will be granted by the Commissioner of Income-tax subject to the following conditions and any other condition which he may prescribe—

(a) The employer shall at the end of each year calculate the income-tax and super-tax due on the income under the head "Salaries" paid to his employees during the year and adjust any excess or deficiency in the month of March, such adjustment being made within the terms of the proviso to sub-section (2) of Section 18 of the Act, *i.e.*, adjustments should be made in each individual case and any excess recovered from one employee should not be adjusted against any short recovery from another.

(b) In the case of an employee leaving service the particulars mentioned above should be sent forthwith to the Income-tax Officer."

Auditor's Certificates Rules, 1932—Amendment to.

Notification No. 1-A (6)/43 dated the 20th November 1943.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely:—

For clause (e) of rule 2 of the said Rules, the following shall be substituted, namely:—

"(e) ' Service as an audit clerk ' means services as an audit clerk in the office of a Registered Accountant entitled, or permitted under sub-rule (3) of rule 40, to train articled clerks and includes any service as an audit clerk in the office of any other Registered Accountant—

(i) which, in the case of any person admitted under part II to the First Examination before the year 1944, was recognized as service as an audit clerk under these Rules, or

(ii) which the Central Government undertook before the 9th September 1939 to recognize as such service."

THE INCOME TAX REPORTS

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1943.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS

v.

THE BAR COUNCIL, MADRAS.

SIR LIONEL LEACH, C. J., and LAKSHMANA RAO, J.

November 9, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 3, 4 (3) (i)—MADRAS BAR COUNCIL—WHETHER AN INDIVIDUAL OR AN ASSOCIATION OF PERSONS—INCOME FROM INVESTMENTS, AND ENROLMENT AND EXAMINATION FEES—WHETHER EXEMPT—COUNCIL APPLYING INCOME FROM INVESTMENTS SOLELY FOR LEGAL EDUCATION—WHETHER INCOME APPLIED FOR CHARITABLE PURPOSES.

The Madras Bar Council was a statutory body whose main functions related to the enrolment of persons as Advocates of the Madras High Court, the rights and duties of Advocates and their discipline and professional conduct. Its duties included the giving of facilities for legal education and training, and the holding and conduct of examinations. Its income consisted of fees paid by persons enrolled as Advocates of the High Court, examination fees paid by apprentices-at-law and interest on investments. The Income-tax authorities treated the Bar Council as an individual and levied tax on its income. The Bar Council claimed total exemption under Section 4 (3) (i) of the Income-tax Act. The Bar Council had in fact been treating its investments and income therefrom as applicable to legal education and a formal statement was made on behalf of the Bar Council that it will utilise its income from investments solely for legal education and for expenses in connection therewith.

Held, (1) *that the Bar Council was an individual or an association of persons within the meaning of Section 3 ;*

(2) *that its income from investments was exempted under Section 4 (3) (i) ;*

(3) *that the income derived from enrolment and examination fee was taxable.*

Case referred to the High Court by the Income-tax Appellate Tribunal, Calcutta Bench, under Section 66 (1) of the Indian Income-tax Act, 1922 (XI of 1922) , as amended by Section 92 of the Indian Income-tax (Amendment) Act, 1939 (VII of 1939), in Application No. 66 R.A. Nos. 5 and 6 Madras of 1941-42 on its file for decision on the following questions of law :—

(1) Whether the income of the Bar Council from the various sources set out in the assessment order is exempt under Section 4 (3) (i) of the Income-tax Act ?

(2) Whether the status of the Bar Council for the purposes of assessment is that of an “individual” or whether it does not come under any of the classes of persons liable to pay income-tax under the Indian Income-tax Act ? and

(3) Whether the whole or any part of the receipts of the Bar Council are income, profits or gains assessable to income-tax ?

Referred Case No. 11 of 1942. The facts of the case appear in the judgment of the Appellate Tribunal.

JUDGMENT OF APPELLATE TRIBUNAL.

Under Section 33 of the Indian Income-tax Act (XI of 1922) the Income-tax Appellate Tribunal, Calcutta Bench, consisting of RAM PRASAD VARMA (Judicial Member) and P. N. S. ARYAR (Accountant Member) delivered the following judgment on 5th November 1941.

“The Bar Council, Madras, has been assessed to income-tax for the years 1939-40 and 1940-41 in respect of its income amounting to Rs. 9,708 and Rs. 11,189 respectively. These two appeals raise common questions of law and will be governed by one judgment given in this appeal No. R.A.A. No. 24 Madras of 1941-42.

2. The Bar Council, Madras, returned the above figures of income under protest to the Income-tax Officer and questioned its liability to pay the tax and the ground firstly, that its case is covered by the exemption mentioned in Section 4 (3) clause (i) of the Income-tax Act and, secondly, that it is not one of the classes of persons liable to pay the tax which are mentioned in Section 3 of the Income-tax Act.

3. The Income-tax Officer held that the Bar Council is not exempt under the provisions of Section 4 (3) (i) of the Income-tax Act and on

the second question, *viz.*, the status of the Bar Council, he held it to be an "Association of persons" and for this view he relied on *Commissioner of Income-tax, Madras v. Salem District Urban Bank Ltd.*¹ and assessed the appellant as an "Association of persons."

4. The Appellate Assistant Commissioner gave the matter a detailed and careful consideration and confirmed the assessment made on the appellant. The Appellate Assistant Commissioner, however, differed from the Income-tax Officer on the question of the status of the Bar Council for purposes of assessment and held it to be an "Individual" within the meaning of Section 3 of the Income-tax Act. He relied on *Currimbhoy Ebrahim Baronetcy Trust v. Commissioner of Income-tax, Bombay*² approved in *Commissioner of Income-tax, Madras v. Salem District Urban Bank Ltd.*¹

5. The appellant has argued the same questions before us and has claimed that his case is covered by the exemption mentioned in Section 4 (3) (i) of the Act on the ground that the object of the Bar Council is to promote legal education. It is further contended that in any case it comes within the exemption on the ground that its object is one of general public utility benefiting the public.

6. The questions which arise for our determination may be stated as below :—

(1) Whether the object of the Bar Council is one which attracts the provisions of Section 4 (3) (i) of the Income-tax Act and whether the object of the Bar Councils Act, by which the Bar Councils are constituted, is to confine its activities to legal education?

(2) Whether the status of the Bar Council for the purposes of assessment is that of an "Individual" or "Association of persons" or whether it does not come under any of the classes liable to pay income-tax under the Income-tax Act.

7. We shall first take up the determination of the question as to what the constitution of the Bar Council is and what are the objects with which the Bar Councils Act has been enacted.

Constitution of the Bar Council, its aims and objects.—The Bar Council is a statutory body and according to Section 3 (2) of the Indian Bar Councils Act it has all the attributes of a body corporate. The same section of the Act enacts as under :—

"Every Bar Council so constituted shall be a body corporate having perpetual succession and a common seal with power to acquire and hold property, both movable and immovable and to contract, and shall, by the name of the Bar Council of the High Court for which it has been constituted, sue and be sued."

The Act, which is No. 38 of 1926, is based on the recommendations of the Indian Bar Committee and the whole object was the unification of the Bar in India, the idea being to have a single grade of practitioners entitled to practise in all Courts. The purpose of the Act is to consolidate and amend the law relating to the legal practitioners. This Act amended the Legal Practitioners Act by Section 19 and certain other Acts and directed its attention more towards defining the duties and rights of the members of the Bar, the regulation, the admission and the conduct of the Advocates.

8. Section 8 of the Act deals with the enrolment of the Advocates and the seniority of the Advocates *inter se*. It further deals in clause 4 with the respective rights, pre-audience of the Advocates of the High Court and the rights of the Advocate-General. The roll of the Advocates has to be prepared by the Bar Council and requires it to be sent to the High Court, and the rules, etc., are to be framed by the Bar Council.

Section 9 deals with the making of rules for regulating the qualification for admission to the roll of the Advocates.

Sections 10 to 13 deal with the enquiries into the conduct of Advocates and the procedure and form of enquiries into the conduct of the Advocates and deal with the manner of constitution of the Tribunal and such other matters.

Section 14 deals with the rights of the Advocate to practise in the High Court of which he is an Advocate and in other Courts subject to rules made by the Bar Council.

Section 15 then deals with the powers to make rules, regulations and duties of the Advocates, their discipline, professional conduct, right to practise and matters connected with providing facilities for education and holding and conducting of the examination. The statute, in the main, deals with the powers of the Bar Council to training, enrolling and qualifying an Advocate for the roll to be prepared for the Council and also for the manner of the enquiries into the conduct of the Advocates. Clause (c) of this section is principally relied on by the learned Advocate of the appellant.

9. It will appear from the above resume of the sections that the advancing of the legal education comes in incidentally, and the advancement of the legal education or research in legal education is not its main concern but it deals with the qualifications to be laid down by the Council and the rules to be laid down for the enrolment of the Advocates. It is with this end in view that the Bar Council may make rules for the education and examination of the candidates for being enrolled as Advocates. The section mainly relied on by the appellant, *viz.*, Section 15, may be reproduced as under :—

Section 15 :—“ A Bar Council may, with the previous sanction of the High Court for which it is constituted, make rules consistent with this Act to provide for and regulate any of the following matters namely :—

- (a) the rights and duties of the Advocates of the High Court and their discipline and professional conduct ;
- (b) the conditions subject to which Advocates of other High Courts may be permitted to practise in the High Court ;
- (c) the giving of facilities for legal education and training and the holding and conduct of examinations by the Bar Council ;
- (d) the charging of fees payable to the Bar Council in respect of the enjoyment of educational facilities provided ; or of the right to appear at examinations held by the Bar Council ;
- (e) the investment and management of the funds of the Bar Council, and
- (f) any other matter in respect of which the High Court may require rules to be made under this section.”

It will appear that the Bar Council may make rules on objects mentioned in clause (c) with the permission of the High Court which may or may not be granted. The University is there to give qualifying tests as far as any other Bar Councils in India are concerned.

10. We will now turn to consider the *conception of Charitable Purposes as given in the Act.*

Section 4 (3), clause (i), so far as relevant reads as under :—

“ Any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes.”

The question is whether the income of the Bar Council derived from property is held under trust or other legal obligation wholly for religious or charitable purposes. The question narrows down to whether the objects as defined in the Act are for education or are for advancement of any other object of general public utility. It is not and it is not contended to be for religious purposes. The word ‘wholly’ used in the section under consideration has some significance and it has been interpreted to mean ‘solely’ and not partly. The Council can claim exemption only if it can show that its sole purpose is education or (2) the advancement of any other object of public utility. It is clear that the whole object is not legal education and the Bar Council is concerned with education only so far as the admission to the profession is concerned. The decisions, which we shall have occasion to consider a little later, go to show that if the main object is to benefit the profession the fact that it incidentally helps education will not make it charitable.

The Income-tax Officer and the Appellate Assistant Commissioner relied on *Sulley v. Royal College of Surgeons*¹ and *The General Medical Council v. Commissioners of Inland Revenue*². The appellant relied on *Commissioners of Inland Revenue v. Forrest (Institution of Civil Engineers)*³ and *The King v. Commissioners for Special Purposes of the Income Tax (Ex parte University College of North Wales)*⁴.

11. It may be pointed out that there is no obligation under the Bar Councils Act to impart legal education. The functions are permissive as will appear from Section 15 mentioned above, and it may be noted that several Bar Councils in India, though the Act has been in force for 15 years, have taken no steps to make rules nor have they done anything towards legal education. It must be said to the credit of the Bar Council, Madras, and its energetic secretary that some work has been done in this direction.

12. The decisions cited below also show that if the main object is to benefit the profession the fact that incidentally it helps education will not make the object charitable. That "public utility" does not include benefit to the members of a profession alone is clear from the decision of the Court of Appeal in the case of the *General Medical Council*⁵. The position of the General Medical Council formed under the Medical Act presents the closest analogy to the Bar Council. Both are created by statute and the object is similar, *viz.*, to regulate a profession. The benefit to the public, if any, is indirect, *i.e.*, only by betterment of the profession. It was held by the Court of Appeal that the Council was not established for charitable purposes only and was not entitled to exemption. The argument in this case was "that this body has been formed for what may be called *general public benefit*, and that it is therefore to be considered as a body which can ultimately be brought within the definition of a charity", See page 844 of the judgment of Lord Hanworth, M. R. The question under the Indian Act is the same. Lord Hanworth states the question which has to be put when one is considering objects of public utility in these words: "Is this a body formed for the promotion of abstract science?", or on the other hand, "Is this a society formed for professional purposes?" He answers the first question in the negative and the second in the affirmative and decides the case in favour of the Crown: page 848.

13. Under the Indian Act also the question is whether the object is one of public utility and the test questions laid down by Lord Hanworth are directly applicable. This is a direct authority for holding that if a society is formed for professional purposes its object is not one of public utility and is not hence charitable. The following

(1) (1892) 3 Tax Cas. 173.
(2) (1928) 13 Tax Cas. 819.

(3) (1890) 3 Tax Cas. 117.
(4) (1909) 5 Tax Cas. 408.

observations of Sargant, L.J., also at page 849 are very pertinent and apply with all force to Bar Councils:—

“I think myself that the whole scheme of this legislation is to regulate the profession of medical men, who in consequence have certain privileges conferred upon them by the legislation and that it is in the first instance as a professional measure that the legislation is to be regarded. No doubt, as I have said, the result of that strict qualification and supervision will be to the public advantage. *Exactly the same thing might be said of the regulations which govern the admission of qualified persons to the ranks of solicitors and barristers, or any other scientific profession.*” This decision is applicable in law and on the facts. There is nothing to distinguish the present case from it.

14. The case which appears at first to favour the Council is the case of *Institution of Civil Engineers v. Inland Revenue*¹. Though the decision of the case was in favour of the assessee, yet the principle laid down is wholly against him; for the case has proceeded upon the footing that if the substantial purpose was to benefit the profession the object would not be charitable. The object was held to be charitable in this case on the express finding based on the facts, that the object of the institution was primarily to advance science and not to benefit the profession. Lord Hanworth, M. R., concludes as follows (page 174):—

“After these careful criticisms and incisive analysis of the object and purpose of the institution and the effect of membership upon engineers who belong to it, the House of Lords held that it was exempt as being carried on for the promotion of engineering science and not for the promotion of professional interest or advantage of the members.” Lawrence, L. J., puts the essence of the matter in these words (page 174): “The answer to this question depends upon whether the institution is established solely for the advancement of the science of civil engineering (an admittedly charitable purpose) or whether one of the purposes for which it is established is to benefit civil engineers in order to enable them to practise their profession to greater advantage.” The *ratio decidendi* of the case instead of helping the Bar Council, goes against it and affirms the principle that if the substantial object of a body is to regulate and advance the interests of a profession, its object would not be charitable.

15. The question of Medical Councils, *The General Medical Council*², *General Nursing Council for Scotland*³, *Institution of Civil Engineers*¹, *Geologists' Association*⁴, and *Juridical Society*⁵, and *Yorkshire Agricultural Society*⁶ have come up before the English

(1) (1931) 16 Tax Cas. 158.

(2) (1928) 13 Tax Cas. 819.

(3) (1929) 14 Tax Cas. 645.

(4) (1928) 14 Tax Cas. 271.

(5) (1914) 6 Tax Cas. 467.

(6) (1927) 13 Tax Cas. 58.

Courts and all these decisions (including the cases where the objects have been held to be charitable) establish that if the substantial object of the institution is to benefit a profession or the members of the institution its purpose would not be charitable, even though incidentally such associations advance the science which the profession practise.

The earliest case in which the position of professional associations was clearly stated is *Commissioners of Inland Revenue v. Forrest*¹. Lord Macnaghten said in this case before the House of Lords: "The question at issue may be stated shortly. Is the property of the Institution of Civil Engineers legally appropriated and applied for the promotion of the science of civil engineering, or is it legally appropriated and applied *for the benefit of Civil Engineers in order to enable them to practise their profession to greater advantage?*" The principle expressed in this case that if the substantial object of an institution is to benefit the members of the profession and not the advancement of education or science, its income would not be exempt has been consistently followed in all later cases.

In *Sulley v. Royal College of Surgeons*², the Royal College of Surgeons, Edinburgh, was held to be not a scientific or literary institution but an institution for the advancement of the profession of Surgeons and its income was held liable to income-tax.

In *Royal College of Surgeons v. Inland Revenue*³, a decision of the Court of Appeal, the College had two main objects, each of great importance. One was the promotion of the science of surgery, and the other the promotion and encouragement of the *practice* of surgery including the promotion of the interest of those practising or about to practise surgery as a profession and also including the examination of students and others to qualify for practice, or honours in surgery and kindred subjects. Their Lordships disposed of the second object summarily with the following words: See page 367. "Now, so far as concerns property which may be legally appropriated and applied to what we have called the second main function of the college as distinguished from its other function of the promotion of the science of surgery, it appears to us clear that such property *would not come within any of the exemptions from duty* mentioned in Section 11 of the Customs and Inland Revenue Act, 1885." This Section 11 of the Customs and Inland Revenue Act, 1885, exempted under sub-section (3) "property which or the income or profits whereof is legally appropriated and applied for the promotion of science."

In *Farmer v. Juridical Society of Edinburgh*⁴, the test to be applied is thus stated in Lord Mackenzie's judgment at page 475 where his

(1) (1890) 3 Tax Cas. 117.

(3) (1899) 4 Tax Cas. 344.

(2) (1892) 3 Tax Cas. 173.

(4) (1914) 6 Tax Cas. 467.

Lordship quotes from the case of *Sulley v. Royal College*¹: "If the main and leading object of the institution be that of advancing the interests of a profession then the fact that it may incidentally and as a consequence promote science, will not the least make it other than a professional institution and as such not entitled to the exemption claimed." In this case even though it was set out in the first section of the Rules of the Society that "the object of the society shall be the advancement of the science of law and the pursuit of general literature," it was unanimously held by three Lords (the Lord President, Lord Mackenzie and Lord Skerrington) that the society was a professional institution.

16. *Findings on the first point.*—There is nothing either in the Indian or English Acts or decisions to support the view that a body like the Bar Council is one established for a charitable purpose. On the other hand every decided case supports the view laid down in the *General Medical Council case*² that the purpose of a body which is constituted for the benefit of a profession is not a charitable purpose even though incidentally it may hold examinations, give lectures, etc., and advance education or science.

Our findings on the first issue, therefore, are that the objects of the Bar Councils which are multifarious do not attract the provisions of Section 4 (3), clause (i), of the Income-tax Act and the Bar Councils are not constituted to confine their activities solely to legal education. If the object of the Bar Councils Act was the promotion of legal science in the abstract just as in the case of *Commissioners of Inland Revenue v. Forrest*³ cited above, the position would have been different. But as stated above the functions primarily are for the benefit of the profession and legal education contemplated in the Act merely qualifies its members for enrolment as Advocates or helps to make better Advocates. The benefit of education is available to the members of the profession and though the general public may be eventually benefited by the Advocates being better equipped in legal knowledge, it is only an indirect and remote purpose and not the immediate one. The object is neither in the nature of general public utility nor does it fulfil any other purpose stated in Section 4 (3), clause (i), of the Income-tax Act.

17. *Findings on the second point.*—We will now devote ourselves to the consideration of the second question. There is a difference of opinion on the question, for the Income-tax Officer held it to be an "Association of persons" and the Appellate Assistant Commissioner held the Bar Council to be an individual. The case which the Income-tax Officer examined and relied upon for his view is *Commissioner of*

(1) (1892) 3 Tax Cas. 173.

(2) (1928) 13 Tax Cas. 819.

(3) (1890) 3 Tax Cas. 117.

*Income-tax, Madras v. Salem District Urban Bank Ltd.*¹, while the Appellate Assistant Commissioner footed himself on *Currimbhoy Ebrahim Baronetcy Trust v. Commissioner of Income-tax*², and observations in *Commissioner of Income-tax, Madras v. Salem District Urban Bank Ltd.*¹

We have gone through all the cases and have come to the conclusion that a corporate body like the Bar Council can more appropriately be classified as an "Individual" rather than an "Association of persons."

The case in *Currimbhoy Ebrahim Baronetcy Trust v. Commissioner of Income-tax*² went on appeal before their Lordships of the Privy Council and is reported in *Currimbhoy Ebrahim Baronetcy Trust v. Commissioner of Income-tax, Bombay*³. The judgment on appeal was confirmed and no exception was taken to the view that the corporate body of trustees was an "Individual" though this specific point was not considered or debated before their Lordships.

Section 3 says—"Where any Act of the Indian Legislature enacts that income-tax shall be charged for any year at any rate or rates applicable to the total income of an assessee, tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of this Act in respect of all income, profits and gains of the previous year of every individual, Hindu undivided family, company, firm and other association of individuals."

The word "individual" has not been used as synonymous with 'persons.' It would have been quite easy to use the word "person" in this section instead of the word "individual" if it was so intended. The word "individual" has been defined in the Oxford Dictionary as:—

"One in substance or essence; forming an indivisible entity; indivisible." The corporate body like the Bar Council fulfills the sense of this word. In *Currimbhoy Ebrahim Baronetcy Trust v. Commissioner of Income-tax, Bombay*³, it was so held. The case of *Commissioner of Income-tax, Madras v. Salem District Urban Bank Ltd.*¹, relied upon by the Income-tax Officer does not decide a contrary proposition. In fact, it supports the view taken in the Bombay case as against the latter view taken by the Bombay High Court in *Commissioner of Income-tax, Bombay v. Ahmedabad Mill-owners' Association*⁴. In the case of *Salem District Urban Bank Ltd.*¹ referred to above, the question for consideration was whether a body like the Salem District Urban Bank, shares of which were held by

(1) (1940) 8 I.T.R. 269.

(2) (1932) 5 I.T.C. 484.

(3) (1934) 2 I.T.R. 148; 7 I.T.C. 195.

(4) (1939) 7 I.T.R. 369.

persons and co-operative societies was an "Individual" or an "Association of individuals" and their Lordships held that the words "Association of individuals" embrace an association of corporate bodies. In the same case under consideration the Chief Justice of the Madras High Court had laid down:—

"To give the word 'individual' the meaning of 'persons' only would, it seems to me, be to disregard the scheme of the Act and to rob the word of an accepted meaning."

We, therefore, feel that the Bar Council can be held to be an "Individual" within the meaning of Section 3 of the Income-tax Act and is a body liable to pay tax on its investments and other incomes as per return.

Conclusions.—We have found above that the income of the Bar Council is not exempt as it is not applied to any educational purposes or any object of public utility within the meaning of clause (i) of Section 4(3). We have also held that it is to be classed for purposes of Section 3 of the Income-tax Act as "Individual."

18. The result is that these two appeals preferred by the Bar Council, Madras, are dismissed and the orders assessing it are hereby confirmed."

On the application of the assessee under Section 66 (1) of the Indian Income-tax Act (XI of 1922) the Appellate Tribunal referred the case to the Madras High Court:—

STATEMENT OF CASE.

"These are two applications of the assessee under Section 66 (1) of the Income-tax Act relating to the assessment for the years 1939-40 and 1940-41 requiring us to refer to the High Court some questions which, it is alleged are questions of law and arise out of our order dated the 5th November 1941, under sub-section (4) of Section 33 of the Act of in regular assessment Appeals Nos. 25 R.A.A. and 24 R.A.A. Madras of 1941-42 respectively. As the facts of the case and questions raised are the same in the said two applications, only one reference is made.

2. The applicant has formulated these questions as follows:—

(i) Whether the Bar Council of the High Court created by statute is not constituted for the performance of duties for the benefit of the public and for the advancement of an object of public utility within the meaning of Section 4 (3) (i);

(ii) Whether the Bar Council is not a "public body" other than an "individual, Hindu undivided family, company, local authority, firm or other association of persons" within the meaning of Section 3 of the Act;

(iii) Whether the Bar Council of the High Court is a council formed for enabling the Advocates to practise their profession with greater advantage to themselves, and is for the benefit of the members of the profession alone and only indirectly for the benefit of the public ;

(iv) Whether the securities and deposits in bank for which Rs. 4,107 interest-income was derived were not property held wholly for charitable purposes within the meaning of Section 4 (3) ;:

(v) Whether the examination fee levied is not in connection with the education and wholly charitable within the meaning of Section 4 (3) (i) ;

(vi) Whether the Bar Council of the High Court can be said to derive "income, profits or gains" within the meaning of the Income-tax Act by reason of statutory fees received from persons enrolling as Advocates.

3. In the reply to the application filed under rule 54 of the Appellate Tribunal Rules, the respondent states that the only questions of law that arise out of the said order are :—

(i) Whether the income of the Bar Council from the various sources set out in the assessment order is exempt under Section 4 (3) (i) of the Income-tax Act ?

(ii) Whether the status of the Bar Council for the purposes of assessment is that of an 'individual' or whether it does not come under any of the classes of persons liable to pay income-tax under the Indian Income-tax Act ?

4. *Statement of the Case.*—The applicant is a statutory body constituted under Section 3 (2) of the Indian Bar Councils Act. For the income-tax years 1939-40 and 1940-41, they were assessed on an income under the head "interest on securities, business and other sources." In this assessment, the income on securities, and the moneys held by the applicant were assessed under the head "interest on securities" and "other sources" respectively; the receipts by way of enrolment fee and the balance of examination fee were assessed as income from business liable to income-tax. The applicant claimed that in respect of the income from securities and moneys held there, they were held under trust or other legal obligation wholly for charitable purposes and as such were exempt within the meaning of Section 4 (3) (i) of the Income-tax Act ; the receipt by way of enrolment fee was not income at all and therefore not assessable and the examination fee was for the purpose of educational facilities and as such was not liable to assessment under Section 4 (3) (i). It was further contended that the Bar Council was formed for professional purposes and conferred benefit on the legal profession as well as on the public and therefore the

purposes served were those of public utility. It is further alleged that the status for the purposes of assessment under the Income-tax Act is neither of an 'individual' nor that of an 'association of persons,' nor could it be covered by any of the several terms mentioned in Section 3 of the Income-tax Act and that its income is not income at all.

5. The Tribunal considered these points and by their order dated the 5th November 1941, came to the conclusion against the contention of the applicant. The reasons for such finding have been fully set out and they need not be repeated here. It was held by the said order that the Bar Council was not exempt as its income was neither applied to any educational purposes nor to any object of public utility within the meaning of clause (1) of Section 4 (3) of the Income-tax Act.

6. It was further held for the purposes of Section 3 of the Income-tax Act that the applicant should be classed as an 'individual.'

7. The question that the surplus of receipts of the Bar Council over the disbursements in the 'previous year' was not income at all was not argued before the Tribunal nor was considered by it. If it should have been argued, the Tribunal would have had no hesitation to hold it as income, as in the case of *Commissioner of Income-tax, Bengal v. Messrs. Shaw Wallace & Co.*¹, disposed of by their Lordships of the Privy Council. Owing to its regular frequency, the income cannot be said to be casual in its nature. Strictly speaking, the question does not arise from our order but as it is implied in it by our confirmation of the assessment, we have no hesitation in referring the question along with others.

8. We think that the following questions of law do arise out of our order. They cover the questions raised by the applicant and we refer them to the High Court of Madras as below :—

(i) Whether the income of the Bar Council from the various sources set out in the assessment order is exempt under Section 4 (3) (i) of the Income-tax Act,

(ii) Whether the status of the Bar Council for the purposes of assessment is that of an 'Individual' or whether it does not come under any of the classes of persons liable to pay income-tax under the Indian Income-tax Act, and

(iii) Whether the whole or any part of the receipts of the Bar Council are income, profits or gains assessable to income-tax?"

K. V. Sesha Aiyangar, for the Commissioner.

Sir Alladi Krishnaswami Aiyar (Advocate-General) and M. Subbaraya Aiyar, for the assessee.

This reference came on for hearing on Monday the 2nd day of November, 1942, and the Court delivered the following :—

JUDGMENT.

(Judgment of the Court was delivered by the Hon'ble the Chief Justice).

The questions referred by the Income-tax Appellate Tribunal relate to the liability of the Bar Council of Madras to income-tax. The Income-tax authorities have imposed a tax on the income of the Council for the years 1939-40 and 1940-41. In the previous years no tax was levied, it being taken that the income of the Council was not taxable under the Act. It may be mentioned that the Bar Councils of Calcutta, Bombay, Allahabad, Lucknow, Patna, Sind and Nagpur have not been required to pay tax on their income. The income of the Council consists of fees paid by persons enrolled as Advocates of the High Court, examination fees paid by apprentices-at-law and interest on investments. The enrolment fees provide the biggest source of income. The income is utilized for meeting the establishment expenses and the payment of fees to lecturers and examiners. The Council is a statutory body whose main functions relate to the enrolment of persons as Advocates of the High Court, the rights and duties of Advocates and their discipline and professional conduct. Its duties, however, include the giving of facilities for legal education and training and the holding and conduct of examinations.

Section 3 of the Income-tax Act which is the charging section makes, *inter alia*, an individual or association of persons liable to pay the tax on income. The Council has been taxed as an individual, and there can be no doubt that it is an individual or association of persons within the meaning of the section. Therefore its income is taxable unless exemption is to be obtained under the provisions of Section 4 (8). Clause (i) of sub-section (3) exempts income derived from property held under trust or other legal obligation wholly for religious or charitable purposes and, in the case of property so held in part only for such purposes, the income applied or finally set apart for application thereto. The last clause of this sub-section defines what is meant by the words "charitable purpose" and the definition includes education.

When the Income-tax Officer proposed to assess the Council to income-tax, it claimed total exemption by reason of clause (i) of the sub-section and the case has proceeded throughout on that basis. The Council appealed from the Income-tax Officer's order to the Appellate Assistant Commissioner and from the latter's order, which confirmed

the Income-tax Officer's order, to the Income-tax Appellate Tribunal, which agreed with the Income-tax authorities that this clause did not exempt the income of the Council.

Now, it is clear that it does exempt income derived from the investments of the Council if those investments are held by the Council for educational purposes. This aspect of the case has not been considered. The learned Advocate-General who appears on behalf of the Council has stated to the Court that the investments of the Council have been made, and the fund represented by them is held, for educational purposes. This being so, this income is not taxable. On the other hand it is quite clear that the income derived from enrolment and examination fees is taxable income. At the suggestion of the Court, the Council will make a formal statement to the Income-tax authorities with regard to the purposes for which the investments are held. In these circumstances Mr. Sessa Ayyangar, on behalf of the Income-tax authorities, suggests that the case may be allowed to stand over for a week in order to enable him to obtain instructions from the Commissioner of Income-tax. We agree to this course and the case will stand out of the list until next Monday. If it is possible, as it appears likely, that an agreement may be arrived at, it will not be necessary for this Court to answer the reference.

This case coming on for further hearing on 9th November 1942 the Court made the following :—

ORDER.

(The order of the Court was delivered by the Hon'ble the Chief Justice).

The learned Advocate-General on behalf of the Bar Council states that the Council will utilize its income from investments solely for legal education and for expenses, including establishment charges, in connection therewith. In future separate accounts will be maintained for this purpose. In past years the Council have been treating the investments and income therefrom as applicable to legal education, though no separate accounts have been maintained in respect of the investments. This makes it perfectly clear that the income of the Council received from investments is not taxable. As we have pointed out in our order, dated the 2nd November 1942, the income from enrolment and examination fees is taxable. The Commissioner of Income-tax accepts the statement of the learned Advocate-General.

In these circumstances the assessment for the years in question should be made on this basis. The questions referred will be answered in the sense indicated in our two orders.

There will be no order as to costs.

Reference answered accordingly.

[IN THE PATNA HIGH COURT.]

SIRDAR BAHADUR INDRA SINGH

v.

COMMISSIONER OF INCOME-TAX, BIHAR AND ORISSA.

HARRIES, C. J., and MANOHAR LALL, J.

September 18, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 3, 25A, 66 (3)—STATUS—INDIVIDUAL OR HINDU UNDIVIDED FAMILY—SUBMISSION OF RETURN AND ASSESSMENT AS HINDU UNDIVIDED FAMILY FOR SEVERAL YEARS—SUBSEQUENT CLAIM TO BE ASSESSED AS INDIVIDUAL—LEGALITY—EVIDENCE TO PROVE THAT BUSINESS IS SELF ACQUISITION—VALUE OF—ABSENCE OF NUCLEUS—PREVIOUS ADMISSIONS IN INCOME-TAX RETURNS—EFFECT—ESTOPPEL—RES JUDICATA—SCOPE OF SEC. 25A (3)—QUESTION OF FACT—INTERFERENCE BY HIGH COURT.

The assessee, who was assessed up to the year 1924 as an individual, claimed before the Commissioner in the year 1924-25 that his assessable income was derived from business which belonged to the joint family consisting of himself, his three sons and his brother. Although the joint family had no nucleus, the assessee was assessed as a Hindu undivided family on the basis of his statement for the first time in that year. In the subsequent years the assessee continued to file returns as a Hindu undivided family and he was also assessed on the same basis. In the year 1935 the assessee, who had by that time built up a large steel works business, transferred that business to a public company in consideration of about Rs. 32 lakhs in the form of shares and debentures of that company. The assessee thereafter formed a private company consisting of himself and his two sons to act as the managing agents of the public company and appointed the private company as his nominee to receive the consideration of Rs. 32 lakhs from the public company. The assessee became the governing director of the private company on a remuneration of Rs. 1,000 per month. In the year 1938-39 the assessee again made a return showing his status as a Hindu undivided family and he was assessed on that basis on an income of Rs. 1,30,805 which included the sum of Rs. 12,000 representing director's fees. The assessee subsequently contended that the whole income should be assessed in his hands as an individual for the following reasons : (1) the joint family had no nucleus and his statement before the Commissioner that the business was joint family business would not make it a joint family business ; (2) the agreement of transfer between the assessee and the public company distinctly provided that the assessee had for some time past been carrying

on the business in his own name and he was the sole proprietor of that business ; (3) the assessee exercised full dominion over the consideration of Rs. 32 lakhs received by his nominee (the private company) which was subsequently divided in three equal parts ; (4) the assessee and his two sons in order to avoid future disputes entered into a family arrangement in 1939 by which the Rs. 32 lakhs was divided in three equal portions ; and (5) the sum of Rs. 12,000 received by him as governing director was his private income. The Commissioner rejected these contentions and confirmed the assessment. On a reference under Section 66 (3) :

Held, (1) that the principle of estoppel or res-judicata has no application to income-tax cases ; but the admissions made by the assessee were pieces of evidence which could be considered to determine the status of the assessee ;

(2) that the joint family had no nucleus and the admission made by the assessee before the Commissioner when construed strictly and literally, and the subsequent declarations in the returns could not convert the separate property of the assessee into joint family property. In any case the recitals in the instrument of transfer of the business to the public company and the subsequent dominion exercised by the assessee over the consideration completely outweighed the effect of the admissions ;

(3) that the Court in arriving at this decision was not interfering with the finding of fact arrived at by the Commissioner but was merely considering the proper legal effect of all the proved facts which had been stated in the reference by the Commissioner and which were admitted by the parties ;

(4) that, as the contention that the family had disrupted by the subsequent arrangement between the assessee and his sons was not put forward before the Income-tax Officer at the time of making the assessment, the family would be continued to be treated under Section 25A (3) as a joint Hindu family for the purposes of the Income-tax Act ;

(5) that under the circumstances the assessee and his two sons constituted a Hindu undivided family ; but the income from the business, property, etc., was not assessable as the income of the joint family but as of the assessee in his individual capacity ;

(6) that the income of the assessee as the governing director of the private company could not be included in the income of the joint Hindu family.

MANOHAR LALL, J.—Title to land cannot pass by an admission when the statute requires a deed.

The property of an individual cannot become the property of a joint Hindu family by mere expression of intention unless the property

is transferred to the joint Hindu family by some means recognised by law. If it is movable property then it should be handed over to the joint family and its subsequent possession or enjoyment should be shown to be on behalf of the joint Hindu family. If it is immovable then it must be transferred by a registered document if its value is more than Rs. 100.

Cases referred to :—

A. L. P. R. Periakaruppan Chetty v. R. M. A. M. Arunachalam Chetty (1926) I.L.R. 50 Mad. 582.

Broken Hill Co., Ltd. v. Municipal Council of Broken Hill [1926] A.C. 94.

Jadu Nath Poddar v. Rup Lal Poddar (1906) 33 Cal. 967 ; 10 C.W.N. 650 ; 4 C.L.J. 22.

Kashi Nath Pal v. Jagat Kishore Acharya Choudhry (1915) 20 C.W.N. 643.

McNelly v. S.R.O. Coy. (1903) 62 L.R.A. 562.

Nafar Chandra Pal Choudhry v. Shukur Sheikh (1918) I.L.R. 46 Cal. 189.

Rai Bahadur Sahu Har Prasad Raja Radha Raman v. Commissioner of Income-tax, C.P. & U.P. (10 I.T.C. 83).

Ram Gopal v. Shamskhaton (1892) I.L.R. 20 Cal. 93 ; 19 I.A. 228 ; 6 Sar. P.C.J. 247 ; 17 Ind. Jur. 38.

Ram Parkash Das v. Anand Das (43 I.A. 73).

Ramratan Sukul v. Nandu (1892) 19 I.A. 1 ; 19 Cal. 249.

Case stated under Section 66 (3) of the Indian Income-tax Act (XI of 1922 before Amendment) by the Commissioner of Income-tax, Bihar & Orissa : (Miscellaneous Judicial Case No. 15 of 1941).

STATEMENT OF CASE.

“In compliance with your above letter,* I have the honour to send herewith a statement of the case under Section 66 (3) of the Indian Income-tax Act of 1922 (referred to hereinafter as “the Act”).

2. The assessee in this case is a Hindu undivided family of Sirdar Indra Singh and his two sons, Sirdar Baldev Singh and Sirdar Ajaib Singh, the “Karta” whereof is Sirdar Indra Singh of Jamshedpur. The income under reference pertains to the “previous” year ending 31-3-1938 (hereinafter referred to as “the accounting year”), which forms the basis of assessment for the financial year 1938-39 hereinafter referred to as (“the assessment year”). We are, therefore, concerned with the Act as it stood before the amendment of 1939. Sirdar Indra Singh has been doing the business of a contractor since a long time at Jamshedpur and also owns some house property. He used to be assessed for and up to the assessment year 1924-25 on the income from these sources as an “individual.” It was in that year that, in connection with his super-tax assessment, he objected to the status, stating that the assessment should have been made as on a “Hindu undivided family.” His contention was allowed by the then Commissioner of Income-tax, Mr. Middleton, as per his review order dated 26-6-1925

* No. 1744 M. A., dated Patna, the 31st March 1941.

(Exhibit A). The assessee accordingly got the advantage of a higher slab of statutory exemption from super-tax to the extent of Rs. 75,000, instead of Rs. 50,000 which was applicable in the case of "individuals." Ever since then, he is being assessed as a "Hindu undivided family" and has been getting the statutory abatement of Rs. 75,000 for super-tax. Even in the assessee's returns of total income filed in the last several years up to the financial year 1939-40 (including the assessment year under reference of 1938-39), the status noted by the assessee was that of a "Hindu undivided family." Relevant extracts from the returns filed in the above years 1934-35 to 1939-40 are given in Exhibits B to G. It is important to note that in the returns for the year 1936-37 (Exhibit D) and 1937-38 (Exhibit E), even the director's fees received in the names of the above-mentioned two sons of Indra Singh and himself were all aggregated and returned as the income of the family. It may also be observed that in order to support his contention that the assessee is not a "Hindu undivided family", he also filed a claim under Section 25 A for the purpose of 1939-40 assessment, stating that on the strength of the agreement dated 24th March 1939 (Exhibit H), the family had already disrupted and that the family properties had been partitioned among Sardar Indra Singh and his said two sons. But, this claim was rejected by the Income-tax Officer.

3. It seems that the contention regarding the assessee's status was not properly argued by the assessee before the Income-tax Officer, as was done before the Assistant Commissioner of Income-tax. As no evidence was produced by the assessee in support of this contention, the Assistant Commissioner did not allow it. (Relevant extract from the appellate order is given in Exhibit I.) The assessee, not being satisfied with the Assistant Commissioner's order, filed an application before me only under Section 66 (2) of the Act, there being no review petition filed under Section 38 of the Act. For the reasons given in my order, dated 9-8-1940 (relevant extract therefrom being given in Exhibit J), I declined to make a reference to the Honourable Court. The assessee having filed an application under Section 66 (3) of the Act, I have been directed by the Honourable Court to state a case upon the following questions.

4. Questions of law :—

(1) Do Sirdar Indra Singh and his two sons constitute a "Hindu undivided family" for the purposes of the Indian Income-tax Act (XI of 1922)?

(2) If the answer to question (1) is in the affirmative, is the income from business, property etc., assessable as the income of the joint family or of Sirdar Indra Singh alone?

(3) Can the income of Sirdar Indra Singh as managing director of Indra and Sons Ltd., amounting to Rs. 12,000 in the year of account, be included in the income of the Hindu undivided family?

5. **Opinion of the Commissioner**—As stated above, Sirdar Indra Singh (the assessee in this case), has been on his own representation before my predecessor, assessed hitherto as an “undivided Hindu family.” Even in his returns of income, he has given full details of the adult members of his joint family, as stated above. In the case of a Hindu father and his sons, it is the ordinary presumption in law that they are joint unless proved to the contrary, and this has not been rebutted in this case. On the contrary there has been an admission year after year of the assessee himself, and also a declaration in the duly verified returns, that the family was a Hindu undivided family up to 1939-40 assessment. Even a claim for separation of the members of the family and partition of the joint family properties under Section 25A of the Act was filed during the assessment proceedings for the subsequent assessment year 1939-40, which was, however, unsuccessful. If the assessee’s family were not joint, it is not understood why the claim for separation and partition under Section 25A of the Act was filed (Exhibit H).

6. Besides, there has been a galaxy of rulings holding that the question whether a Hindu family had split up or not is one of fact. It was so held by the Calcutta High Court in the case of *Bisheshwar Lal Brijlal*¹; by the Lahore High Court in the case of *Jattu Shah*²; by the Patna High Court in that of *Ghanshyam Das Ramkumar*³; by the Lahore High Court in *Raja Singh Obera*⁴; by the same High Court in the case of *Piyare Lal and Others*⁵; and by the Rangoon High Court in the case of *Bansidhar and Sons*⁶. In view of these rulings and the facts of the case as given above, and in the absence of any evidence to the contrary, there can be no doubt that the family is undivided.

7. It had also been urged by the assessee that the business and the property in question were the self-acquired property of Sirdar Indra Singh, but no evidence in support thereof was produced before the Income-tax department. On the contrary, it is evident from the facts on record and from his own declarations made by the assessee in his returns from year to year, that Sirdar Indra Singh’s property and earnings were thrown into the common stock of the family. His sons are also grown up and have got good training and experience in business and have been evidently throwing their earnings in the common stock. It was held by their Lordships of the Privy Council in the case of

(1) (1930, 4 I.T.C. 365.

(2) (1932) 6 I.T.C. 162.

(3) (1932) 6 I.T.C. 198.

(4) (1934) 2 I.T.R. 331.

(5) (1933) 1 I.T.R. 215.

(6) (1938) 6 I.T.R. 95.

*Kalyanji Vithal Das*¹ that it was not proved in that case that the individual member had thrown into the common stock his self-acquired property and consequently the income could not be held to be that of the family. The obvious inference of these observations is that, if such an income had been thrown into the common stock of the family it would have been held to be the income of the family. This fact has been proved in this case by the admissions and the representations of the assessee himself year after year. It is also indicated by the fact as explained in para. 10 below, that Sirdar Indra Singh nominated the private company, of which the shareholders were his two sons and himself, to be the recipient of the consideration of Rs. 32 lacs to be given by the public company for the sale of the business of the Indian Steel and Wire Products thereto. If this business were the individual property of Sirdar Indra Singh, he would have himself got the consideration money (which comprised of shares and debentures) and he would not have asked the public company to give that consideration to the private company in which his two sons were also the shareholders with himself in equal shares. It will also appear from the deed of agreement dated 24th March 1939, filed in support of the assessee's claim under Section 25A that Sirdar and his two sons were a Hindu undivided family when the deed was entered into and signed by them.

8. In view of the above facts, it is submitted that there were sufficient material and evidence before the Income-tax department to come to the finding that the assessee is a "Hindu undivided family." In my humble opinion, the first question should, therefore, be answered in the affirmative, *viz.*, to the effect that Sirdar Indra Singh and his two sons constitute a Hindu undivided family for the purposes of the Indian Income-tax Act, 1922, and the second question be answered to the effect that the income from business, property, etc., is assessable as income of the joint family and not of Sirdar Indra Singh alone.

9. As regards the third question, whether the income of Sirdar Indra Singh as managing director of the private company, amounting to Rs. 12,000 in the year of account, be included in the income of the Hindu undivided family, it would be necessary to go into the previous history of the assessee in order to appreciate this question. Sirdar Indra Singh (as the "Karta" of the family) also owned a business called "The Indian Steel and Wire Products", which was sold by him sometime in the year 1935 as a going concern to a public limited company at Calcutta called "The Indian Steel and Wire Products, Limited", (hereinafter referred to as "the public company") for a consideration of Rs. 32 lacs. Really speaking, it was a mere conversion

of a private concern into a public limited company. This sum of Rs. 32 lacs was not to be paid in cash, but in the shape of shares and debentures of the public company. In the ordinary course, Sirdar Indra Singh (as the "Karta" of the family) who was the vendor of the business should have himself received the said consideration (*i.e.*, shares and debentures) of Rs. 32 lacs from the public company. In that case, the assessee (Hindu undivided family) should have also received and accounted for the big dividend and interest from such shares and debentures in the returns of income of the family. Similarly, the Hindu undivided family in the ordinary course would also have been appointed the managing agents of the public company if the private company of Indra Singh and Sons Limited had not been formed by Sirdar Indra Singh, and in which case the assessee would have also received and accounted for the big managing agency remuneration receivable from the public company in the returns of income of the family. But, as stated to me by Sirdar Indra Singh at the time of the hearing of the application under Section 66 (2), because his two sons were with him in the old private business of the Indian Steel and Wire Products and because he wanted to give them a portion of this sale consideration of Rs. 32 lacs, he formed a private limited company at Calcutta called "Indra Singh and Sons Limited" the only three share-holders whereof are also Sirdar Indra Singh and his said two sons, *viz.*, the adult members of the family, in equal shares.

10. Now, if Sirdar Indra Singh wanted to give a part of the said sale consideration to his two sons for settling them in life, as stated above, he could have as well done so by transferring to them some of the said shares and debentures after they were issued to him by the company. But, he said to me that he was advised to form the private limited company which would be a better show. He also told me that he wrote a letter to the public company to issue its shares and debentures of the value of Rs. 32 lacs not to himself (*i.e.*, the Hindu undivided family) as per the memorandum of association of the public company but to his nominees, *viz.*, the private company of Indra Singh and Sons Limited consisting of himself and the two sons. Accordingly, the public company issued the shares and debentures of the value of Rs. 32 lacs to the private company and not to the Hindu undivided family. It was also stated to me by Sirdar Indra Singh that the private company was originally started with a paid up capital of only Rs. 2,000. But later on at his own desire, its share capital was increased to Rs. 30 lacs, not as paid up in cash but by a mere transfer entry of Rs. 29,98,000 from the personal account of Sirdar Indra Singh to the share capital account, in the private company's ledger.

11. Instead of the share capital of Rs. 30 lacs being owned by the Hindu undivided family who were really the owners of this private company, the share capital was issued, as per the wish of Sirdar Indra Singh, in the individual names of the three members of the family, *viz.*, Sirdar Indra Singh and his said two sons in equal shares, *viz.*, Rs. 10 lacs to each of them. The result was that the two sons of Sirdar Indra Singh, *viz.*, Sirdar Baldev Singh and Sirdar Ajaib Singh, without paying a single pie automatically became the owners of (each of them to the extent of one-third) the shares and debentures of Rs. 32 lacs issued by the public company to the private company on account of the said consideration for the sale of the old business of the Indian Steel and Wire Products, the remaining one-third being owned by Sirdar Indra Singh himself. Besides, Sirdar Indra Singh, in his return of income (dated 14-7-1937) for the year 1937-38 had not only declared himself as a "Hindu undivided family" along with his said two sons, but had also shown therein the aggregate of the director's fees of all the 3 members of the family (*viz.*, himself and his sons), even including the amount of Rs. 12,000 which was said to have been received by him as managing director's remuneration from the private company. Similarly, in the return of income for the year 1936-37, the director's fees of Sirdar Indra Singh and his son Sirdar Baldev Singh had been added together and shown as the income of the family.

12. It may not be out of place to add that on a reference being made by the Commissioner of Income-tax, Bengal, to the Board of Referees under Section 23A of the Act as it stood before the assessment of 1939 regarding 1937-38 assessment, the Board held that the private company at Calcutta was practically a one man show, that the company may not be assessed as a separate entity and that its three share-holders (Sirdar Indra Singh and his 2 sons), who are also the members of the joint family, could be assessed directly on the income of the private company under that section.

13. The ultimate effect of all such special arrangements with the public company and the book entries in the private company was that the Hindu undivided family of Sirdar Indra Singh did not show in their own return of income, the big amounts of interest and dividend received on account of the above-mentioned shares and debentures of the value of about Rs. 32 lacs and so also the handsome managing agency remuneration receivable from the public company. All this big income was, however, shown in the return of the private company. It will also be seen from the above facts that the owners of the private company are identical with those of the Hindu undivided family, *viz.*,

Sirdar Indra Singh and his two sons. Therefore, all the net assets of the private company including the shares and debentures of the public company worth about Rs. 32 lacs, truly speaking belong entirely to the Hindu undivided family. The whole of the big income of the private company can, therefore, be appropriated by Sirdar Indra Singh and his two sons, who also form the said Hindu undivided family, in any way they like. It is also seen that the intention of Sirdar Indra Singh in forming the private company was to remove and transfer a portion of the capital or wealth of the Hindu undivided family (together with its income) to the private company, so that for super-tax purposes a portion of the income of the Hindu undivided family may be assessed separately in the hands of the private company at the lower rate, thereby saving a lot of super-tax to the Hindu undivided family and also saving income-tax at the higher rate on the rest of the income of the family.

14. Having once proved that the owners of the private company and the Hindu undivided family are identical, *viz.*, three shareholders and adult members of the family, it is quite clear that the sum of Rs. 12,000 per annum received by Sirdar Indra Singh (and so also in subsequent years by his two sons) from his own private company is not the income of Sirdar Indra Singh alone in his individual capacity, but that it is received by him as a nominee of the Hindu undivided family and also as the director (also share-holder) of his own private company. In view of the fact that the three directors of the private company and also its three share-holders, *viz.*, Sirdar Indra Singh and his two sons were identical, I submit that the department was justified in coming to the conclusion that the sum of Rs. 12,000 was an appropriation of the company's income (*Aspro Ltd. v. Commissioner of Taxes*¹) the person fixing the amount and the person receiving the same being the same person. It was a mere diversion of the company's income and the owners of the company and the adult members of the assessee's Hindu undivided family are also identical. Besides, it was held by the Calcutta High Court that the question, whether payment to a director was *bona fide* for service rendered by him or was a mere distribution of profit to evade assessment of income-tax at proper rates, was one of fact: *Lakshmi Narayan Sen & Sons Ltd., In re*².

15. In the light of the above findings of fact, it is humbly submitted that this third question should be answered in the affirmative."

S. C. Isaacs, S. N. Bose and S. K. Sirkar, for the assessee.

S. M. Gupta, for the Commissioner.

JUDGMENT.

MANOHAR LALL, J.—This is a reference by the Commissioner of Income-tax, Bihar and Orissa, under Section 66 (3) of the Indian Income-tax Act.

It is common ground that Sirdar Indra Singh and his two sons, Sirdar Baldev Singh and Sirdar Ajaib Singh were members of a joint Hindu family up to 1935, but there is a serious dispute between the assessee and the Income-tax department as to whether this Hindu undivided family had joint family property the income whereof was the subject of assessment to income-tax in a number of years and particularly in the year of assessment 1938-39 for the accounting period 1937-38 with which this reference is concerned. In that year Sirdar Indra Singh, the assessee, made a return showing his status as of a Hindu undivided family and was assessed on a total income of Rs. 1,30,805. He contended at the time of the making of the assessment that he should be assessed as an individual and not as joint Hindu family. This contention does not appear to have been clearly raised before the Income-tax Officer but was allowed to be raised in the appeal before the Appellate Assistant Commissioner who overruled the contention and held that the status of the assessee was that of a Hindu undivided family. In the assessable income the Income-tax Officer included a sum of Rs. 12,000 as director's fees received by Sirdar Indra Singh on behalf of the joint Hindu family in circumstances to be described fully hereinafter. The assessee's objection that this was his own private income and not the income of the joint Hindu family was overruled both by the Income-tax Officer and by the Assistant Commissioner who dismissed the appeal on the 29th December, 1939. It may be observed here that the assessee had objected to the inclusion of two other items, (1) Rs. 185-6-6 received from the Indian Steel and Wire Products, Ltd., and (2) Rs. 5,000 which was said to belong to one A. N. Biswas. The assessee failed in getting these two items excluded from his assessable income and the questions now framed do not cover these two items of income and so nothing further need be said about them. Thereafter the assessee moved the Commissioner of Income-tax to refer to the High Court under Section 66 (2) of the Act certain questions of law formulated by him, but the Commissioner on the 9th August, 1940, held that these questions were questions of fact and declined to make a reference. The assessee thereafter moved this Court when the following three questions of law were formulated upon which the Commissioner of Income-tax was asked to state a case:—

“(1) Do Sirdar Indra Singh and his two sons constitute a “Hindu undivided family” for the purposes of the Indian Income-tax Act (XI of 1922) ?

(2) If the answer to question (1) is in the affirmative, is the income from business, property, etc., assessable as the income of the joint family or of Sirdar Indra Singh alone?

(3) Can the income of Sirdar Indra Singh as managing director of Indra Singh and Sons Ltd., amounting to Rs. 12,000 in the year of account be included in the income of the Hindu undivided family?"

The Commissioner sent up a statement of the case on the 2nd of June, 1941.

The assessee who is a very wealthy man started his career years ago as a private contractor in Jamshedpur and by his personal exertions built up a large lucrative and expanding business. Before the year 1924 the assessee used to be assessed to income-tax as an individual. The joint Hindu family at that time consisted of himself, his three sons and his brother, Sirdar Hira Singh, but the family had no nucleus (see the statements in paragraphs 2 and 3 of the petition of the assessee to this Court at page 13—these facts were accepted as correct in the course of the argument before us). On the 26th June, 1925, the assessee moved the Commissioner of Income-tax under Section 38 of the Act to revise the assessment which had been made treating his income as that of an individual. He claimed before the Commissioner that his assessable income was derived from business which "belongs to him and his three sons and his brother Sirdar Hira Singh," that his father is alive but is separate from Hira Singh and Indra Singh and live with their step-mother, that the father and the sons by one wife are joint and the two sons by another wife are joint with each other but separate from their father and step-brothers. The Commissioner by an order dated the 25th June, 1925, (printed at page 8) while disposing of this application for revision of the assessment held that the assessment will be made on Rs. 60,000, but with regard to the claim that no super-tax should be levied because the business was that of a joint Hindu family he observed that as it was impossible to disprove the statement of the assessee, which I have summarised just now, although the only evidence was the assessee's statement, no super-tax should be charged. The effect of this order was that the assessee was assessed for the first time in 1924-25 under the status of a Hindu undivided family. In the subsequent years the assessee continued to be assessed on the same status as a Hindu undivided family and indeed he filed returns, which are required to be submitted each year, on the same basis. It may be stated here that since 26th June, 1925, nothing further has been heard of Sirdar Hira Singh. He appears to have dropped out completely from the assessment records of the Income-tax department. As years rolled on, the business of the assessee grew

still further and in 1935 he or the family owned the Indian Steel and Wire Products Works. Towards the end of that year this concern ceased to exist and its assets were transferred to a public company with limited liability. The memorandum of the company shows that Sirdar Indra Singh, his two sons, Sirdar Ajaib Singh and Arjan Singh and four other persons, were the first subscribers. The capital of this company was fixed at Rs. 50,00,000 divided into 45,000 ordinary shares of Rs. 100 each and 20,000 deferred shares of Rs. 25 each (see paragraph 5 of the memorandum). In the articles of association it is distinctly provided that this limited company was formed to forthwith enter into an agreement with Sirdar Indra Singh in terms of a draft agreement which was then ready. A formal agreement was actually entered into on the 8th February, 1936 (marked exhibit 1 in this Court), between Sirdar Indra Singh and Indian Steel and Wire Products Limited wherein it was agreed after referring to the relative clauses in the articles of association that a sum of Rs. 32,00,000 being a portion of the consideration for the sale of the goodwill and assets of Indian Steel and Wire Products shall be paid to the vendor Sirdar Indra Singh in this way: Rs. 5,00,000 by the issue to the vendor or his nominees of 20,000 fully paid deferred shares in the capital of the company of Rs. 25 each, Rs. 17,00,000 by the issue to the vendor or his nominees of 17,000, fully paid ordinary shares in the capital of the company, and the balance of Rs. 10,00,000 by the issue of first mortgage debentures of the company carrying interest at the rate of Rs. seven and half per cent. per annum. In the recitals it is distinctly and clearly stated that the vendor has for some time past in his own name or as the sole proprietor of Indra Singh and Sons carried on business as the manufacturer of and dealer in steel wire products at Jamshedpur under the name and style of the "Indian Steel and Wire Products." There is no statement that the assessee was the Karta of any joint Hindu family and that he was entering into this large scale transaction on behalf of his joint Hindu family. (This deed of agreement was tendered on behalf of the assessee and marked as an exhibit in the case without objection by the learned counsel for the Income-tax department. The contents of this document were freely used by the Commissioner in preparing his statement of the case and, therefore, it was thought necessary to have it on the record).

On the 2nd of December, 1935, Sirdar Indra Singh and his son Sirdar Baldev Singh became the first two subscribers of a memorandum of association to form a private company. This company was styled Indra Singh and Sons Limited—the memorandum and articles of association are on the record. Although the subscribers were Sirdar Indra Singh and Sirdar Baldev Singh it is common ground that Sirdar Indra Singh

and his two sons, the third son was dead by this time, were the shareholders of this private limited company which was duly registered under the Indian Companies Act of 1913. The capital of this private company was Rs. 30,00,000 divided into 3,000 shares of Rs. 1,000 each and this company was to act as the managing agents of the Indian Wire and Steel Products Company, Limited, hereinafter to be referred to as the "Public Company." Sirdar Indra Singh nominated Indra Singh and Sons Limited as his nominee to receive Rs. 30,00,000 from the public company as per agreement dated the 8th February, 1936. This sum was divided by the vendor into three parts of Rs. 10,00,000 each between himself and his two sons who, as stated just now, were the only three shareholders of this private company. By article 111 of this company Sirdar Indra Singh was appointed as a governing director until he resigns the office or dies or ceases to hold at least 10,000 shares. By article 116 his remuneration while he held the office of the governing director was fixed at the rate of Rs. 1,000 a month so that his annual emolument was Rs. 12,000 which forms the subject of question No. 3 to be answered by this Court. In the year 1938-39 the assessee came to be assessed as already stated on his income for the previous year 1937-38. The assessment was made on the 30th December, 1938. The appeal against this assessment was disposed of on the 29th December 1939. In the meantime on the 24th of March, 1939, Sirdar Indra Singh and his two sons entered into an agreement which is described as memorandum of agreement between the father and his two sons and is exhibit H (at page 10). It recites that Sirdar Indra Singh by his own exertion and out of his own income has acquired various properties in British India and has been enjoying the rents, issues and profits thereof, that the parties have been living as members of the joint Hindu family, that a number of shares which originally stood in the name of Sirdar Indra Singh were transferred to a private limited company, Indra Singh and Sons Limited, and that these shares have been divided into three parts of Rs. 10,00,000 each, but as differences have arisen between the parties regarding the joint character, management, alienation and distribution of the income of a number of properties including the shares of Indra Singh and Sons Limited, so the parties in order to avoid ruinous and costly litigation have entered into this family arrangement. In the first paragraph it is provided that the properties described in Part I of the schedule standing in the name of Sirdar Indra Singh are his separate and self-acquired properties. Similarly in subsequent paragraphs reference is made to properties detailed in Parts 2 and 3 of the schedules as belonging separately to the other two sons.

In the year of assessment 1939-40, that is subsequent to the year with which the present case is concerned, Sirdar Indra Singh filed an application under Section 25A of the Indian Income-tax Act and relied upon this deed of agreement in support of his claim that the assessee cannot be assessed as a member of a joint Hindu family.

Such in brief is a survey of the facts which have been relied upon by the Commissioner in the statement of the case to come to the conclusion that Sirdar Indra Singh and his two sons constitute a Hindu undivided family for the purpose of the Indian Income-tax Act, 1922, and, therefore, he invites that the answer to the first two questions should be in favour of the department. The assessee on the other hand contends that the Commissioner's finding, apparently a finding of fact, is vitiated by errors of law in that the Commissioner has thrown the onus upon the assessee to prove that the property or business which produced the assessable income in the year of assessment is his private property and has misconstrued the legal effect of the admissions of Sirdar Indra Singh before the Commissioner in 1925 and in the subsequent years. It is also contended that the admission made before the Commissioner in 1925 was due to a misapprehension of the legal position or it might have been an incorrect statement deliberately made to avoid payment of super-tax and that the subsequent declarations which were made in the several years of assessment were similarly being made inadvertently and the draftsman of the various returns simply copied out the statement from the earlier assessment orders. It is argued that when it is the admitted case that this joint Hindu family had no nucleus, the mere statement of Sirdar Indra Singh that the business was a joint family business will not make it a joint family business or the property a joint family property unless the business or the property was transferred to the joint family in a manner recognised by law. It is pointed out that the Commissioner has failed to consider the effect of the various documents which went to form the limited companies in 1935 or the deed of agreement of the 8th February, 1936, or the family arrangement of March, 1939, and, therefore, the Commissioner erred in law when he stated that the assessee has produced no evidence to support his claim that the business or the property was the self-acquired property of Sirdar Indra Singh. Objection is also taken to the Commissioner's observations that the assessee's sons who were grown up and of good training and experience in business "have been evidently throwing their earnings in the common stock." It is claimed that there is no evidence whatsoever to show that the assessee's sons have been throwing their earnings in the common stock. Mr. Isaacs, who argued the case on behalf of the assessee, also submitted

that even if the business and the property be considered to be that of a Hindu undivided family the effect of the transaction in 1935 was to disrupt the joint family so that the family could no longer be treated in law as a Hindu undivided family from February 1936, and, therefore, in the year of assessment the status of the assessee in law was that of an individual.

Learned Counsel on behalf of the Income-tax department on the other hand argues that the question whether the property and business of the assessee is his self-acquisition or whether it belongs to the admitted joint Hindu family is a question of fact and the Commissioner's finding must be accepted by this Court as correct. It is also argued that the assessee is bound by the admissions which he clearly made before Mr. Middleton in June 1925, that the admission was made deliberately with full understanding of its consequences and indeed with the deliberate object that it should be acted upon. It is urged that the assessee cannot complain that his own statement has been accepted as correct and has been acted upon to his advantage and to the detriment of the revenue since 1925. It is pointed out that there could not have been any mistake or inadvertence in making the assertions in 1925, because the assessee repeatedly relied upon the same statement in the subsequent years of assessment and indeed in the very year of assessment now under consideration. In all these years the returns which had to be filed as provided by the Act were duly verified either by or on behalf of the assessee. With regard to the alternative argument advanced on behalf of the assessee the answer put forward is that the provisions of Section 25A (3) of the Indian Income-tax Act are a bar to its being held that the status of the assessee is other than that of a Hindu undivided family.

It must be observed at the outset that the principle of estoppel or *res judicata* has no application in income-tax cases. This has been well settled both in England and in India and reference need only be made to the well known case of *Broken Hill Co., Ltd. v. Municipal Council of Broken Hill*¹ where Lord Carson in delivering the judgment of their Lordships of the Judicial Committee observed at page 100 that the decision of the High Court in an earlier year which was sought to be treated as a final decision binding between the parties was not a final decision because it "related to a valuation and a liability to a tax in a previous year, and no doubt as regards that year the decision could not be disputed. The present case relates to a new question, namely, the valuation for a different year and the liability for that year. It is not *eadem questio*, and therefore the principle of *res judicata* cannot

(1) [1926] A.C. 94.

apply." There are a number of decisions of the Indian Courts to the same effect (see for instance *Rai Bahadur Sahu Har Prasad Raja Radha Raman v. Commissioner of Income-tax, Central and United Provinces*¹). There is therefore no estoppel against the assessee but the admissions made by Sirdar Indra Singh before the Commissioner in 1925 and the subsequent admissions made by him in the later assessment proceedings are undoubtedly pieces of evidence in the case which can be considered to determine the status of the assessee.

To begin with it may be recalled that up to 1925 Sirdar Indra Singh was being assessed as an individual. I have already stated that it is the common case before us that the joint Hindu family of Sirdar Indra Singh and his sons had no nucleus. It must, therefore, be taken that the assessee was being assessed correctly as an individual up to 1924. What happened in 1925 is to be gathered only from the concluding portion of the order of Mr. Middleton while disposing of a revision application of the assessee under Section 33 of the Indian Income-tax Act. Unfortunately the exact statement made by Sirdar Indra Singh has not been produced on behalf of the Income-tax department. It has been held in a number of cases that the recitals in a judgment are no evidence whatsoever to prove the exact admission made by a party or a witness unless the whole of the statement is recited therein. This is based on a good principle because it may be that the Court has taken an incorrect view or has misunderstood the admission made. In *Kashi Nath Pal v. Jagat Kishore Acharaya Choudhury*² a Division Bench of the Calcutta High Court pointed out at page 644 that "the principle is that all judgments are conclusive of their existence, as distinguished from their truth; judgments, as public transactions of a solemn nature, are presumed to be faithfully recorded. Every judgment is, therefore, conclusive evidence, for or against all persons whether parties, privies, or strangers, of its own existence, date and legal effect, as distinguished from the accuracy of the decision rendered; in other words, the law attributes unerring variety to the substantive as opposed to the judicial portions of the record." Attention may also be drawn to the remarks made by Lord Shaw of Dunfermline when delivering the judgment of the Board in the case of *Ram Parkash Das v. Anand Das*³. In that case one of the disqualifications relied upon to invalidate the right of the mahant was that he had entered into a tie of marriage, but this fact was in dispute. In order to prove this fact reliance was sought to be placed upon the statement in a judgment in a criminal case in the course of trial whereof it was alleged that a person who knew the circumstances made a statement on oath that defendant No. 2 was a married man.

(1) 10 I.T.C. 83, at p. 91.

(2) 20 C.W.N. 643.

(3) 43 I.A. 73.

The Magistrate who tried the case stated in his judgment that an admission of the marriage was made in the course of it. Their Lordships held that the note of the admission made to the Magistrate in the criminal case was rightly rejected as not being by itself evidence of the fact recorded therein (page 81).

Assuming however that Mr. Middleton correctly understood the statement which was made to him by Sirdar Indra Singh what was that statement? It was merely this that the business is that of a Hindu undivided family and belongs to Sirdar Indra Singh and his three sons and his brother Hira Singh. It is not stated clearly in the admission that the business from the very start was of an undivided Hindu family. The admission must be construed literally and strictly and so construed it can safely be assumed to mean that, at the time when the statement was made, or in the year of accounting for which the assessment was being made, the business was that of a Hindu undivided family. Can such a statement convert the business into the business of a joint Hindu family?

The Commissioner has expressed the view that it is evident from this declaration that the property and earnings of Sirdar Indra Singh were thrown into the common stock of the family, but, in my opinion, this was an erroneous view to take in law. It is well settled that title to land cannot pass by an admission when the statute requires a deed (see the case of *Jadu Nath Poddar v. Rup Lal Poddar*¹) where reference is made to *McNeelly v. S. R. O. Co.*² Learned Counsel for the assessee relied upon the case of *A. L. P. R. Periakaruppan Chetty v. R.M.A.R. Arumachalam Chetty*³ where Reilly, J., observed that "the separate property of a Hindu ceases to be his separate property and acquires the characteristics of his joint family or ancestral property, not by any physical mixing with his joint family or ancestral property, but by his own volition and intention, by his waiving or surrendering his special right in it as separate property" and further a few lines later that "a man's intention can be discovered only from his words or from his acts and conduct. When his intention in regard to his separate property is not expressed in words, we must seek it in his acts and conduct, in the way in which he has dealt with the property or has allowed others to deal with it." He, therefore, contends that the mere statement made by Sirdar Indra Singh to the Commissioner of Income-tax was not a clear expression of intention within the meaning of Hindu law because such an expression of intention should have been made to other members of the joint Hindu

(1) (1906) 33 Cal. 967, at p. 984.

(2) (1903) 62 L.R.A. 562.

(3) (1926) I.L.R. 50 Mad. 582, at p. 591.

family. He submitted that there is no dispositive document in this case by which Sirdar Indra Singh transferred the property—his own property—to the joint Hindu family. I agree with this contention. The property of an individual cannot become the property of a joint Hindu family by mere expression of intention unless the property is transferred to the joint Hindu family by some means recognised by law, for instance if it is movable property then it should be handed over to the joint family and its subsequent possession or enjoyment should be shown to be on behalf of the joint Hindu family, or if it is immovable then it must be transferred by a registered document if its value is more than Rs. 100. The subsequent declarations made by Sirdar Indra Singh from time to time cannot have a higher value than the original declaration of 1925 because it is not the case of the Income-tax department that anything further was done by Sirdar Indra Singh after he made the statement before Mr. Middleton in 1925 beyond mere declarations in the subsequent assessment proceedings.

Again the Commissioner has not considered the effect of the subsequent documents of 1935-36 and 1939 and was wrong in thinking that no evidence was produced on behalf of Sirdar Indra Singh that the property in question was his self-acquired property. The recitals in these documents and the transactions evidenced thereby are good evidence to show that the property was the self-acquisition of Sirdar Indra Singh. If the Commissioner had found that the elaborate machinery which was adopted by the assessee in 1935, by which he transferred Indian Steel and Wire Products Works to a public company and received the consideration and formed another company to become the managing agents of the public company, was a mere sham transaction, the matter would have been different. But the Income-tax department themselves treated these transactions as real transactions valid in law because they took action under Section 23A of the Indian Income-tax Act regarding the assessment of 1937-38 and proceeded to tax the individual shareholders that is to say Sirdar Indra Singh and his two sons on the undistributed income received by the private company. All the three assessees, Sirdar Indra Singh and his two sons, preferred three separate appeals against the order of the Income-tax Officer which was heard by a Board of Referees who decided on the 12th July 1940 that the Income-tax Officer was justified in invoking the aid of Section 23A (2). They held that the financial position of the company warranted a declaration of dividends and it could have declared dividends by calling upon its principal shareholder—Mr. Sirdar Indra Singh—who happens to be the managing director, to make repayments of his debts (see exhibit 2 of this Court). The Commissioner on

the other hand relied upon this decision of the Board of Referees as if it held "that the private company at Calcutta was practically a one man show, that the company may not be assessed as a separate entity and that its three shareholders (Sirdar Indra Singh and his 2 sons), who are also the members of the joint family, could be assessed directly on the income of the private company under that section" (see paragraph 12 of the statement of the case at page 21). This is a misapprehension of the decision of the Board of Referees. As the Commissioner had relied upon this decision but had not sent up the actual decision of the Board of Referees we have admitted this upon the record of this case with the consent of both parties and have marked it as exhibit 2.

The Commissioner appears to have fallen into a serious error in treating the shareholders of the company as equivalent to the company itself.

The Commissioner has nowhere considered that the public company was specifically formed to acquire the assets of the Indian Steel and Wire Products Company nor has he considered the recitals in the deed of agreement of February, 1936, nor has he considered that the two sons of Sirdar Indra Singh along with the other members of the public in different walks of life were the subscribers to the formation of the public company and that the two sons were subscribers of the private company. It is inconceivable that a public company which was floated in Calcutta with such publicity on such a large scale and acting through well-known solicitors would have entered into this transaction of the purchase of the properties of the value of about 39 lakhs of rupees without investigating the title of the vendor that he was the sole owner of the business and the property hereinbefore carried in the name of Indian Steel and Wire Products Company. In my opinion the effect of these recitals is to completely outweigh the effect of the admission which was made by Sirdar Indra Singh before the Commissioner in 1925, the legal effect of which I have already considered above. Again, the Commissioner has not considered that Sirdar Indra Singh exercised full dominion over the consideration which he received as a result of the transfer to the public company to the knowledge of his sons. He had the power on that date to appoint his nominees to receive the consideration in full or in part and this was actually done by transferring Rs. 30,00,000 of the consideration to the private company. The Commissioner fell into an error when he observed at page 19, line 40, that "if this business were the individual property of Sirdar Indra Singh, he would have himself got the consideration money (which comprised of shares and debentures) and he would not have asked the public company to give that consideration to the private company

in which his two sons were also the shareholders with himself in equal shares." This is a complete misapprehension of the true position. The consideration was received by Sirdar Indra Singh as it was open to him to ask the vendee to pay a portion of the consideration to anybody else and a payment would result in an effectual discharge of the obligation of the vendee.

For these reasons I am of opinion that the Commissioner of Income-tax erred in law in holding that the property and the business in question belonged to the joint family and not to Sirdar Indra Singh alone so that the income derived therefrom in the previous year was assessable in the year of assessment as the income of Hindu undivided family.

This Court is not interfering with the finding of fact by the Commissioner but is merely considering the proper legal effect of all the proved facts which have been stated in the reference by the Commissioner and which were admitted by the parties. Lord Buckmaster in delivering the judgment of their Lordships of the Judicial Committee in *Nafar Chandra Pal Choudhry v. Shukur Sheikh*¹ observed at p. 195 : "Questions of law and of fact are sometimes difficult to disentangle. The proper legal effect of a proved fact is essentially a question of law, so also is the question of admissibility of evidence and the question of whether any evidence has been offered on one side or the other ; but the question whether the fact has been proved, when evidence for and against has been properly admitted, is necessarily a pure question of fact." In *Ramgopal v. Shamskhatoon*², Sir Richard Couch in delivering the judgment of the Board referred with approval to the dictum of the Judicial Committee in *Ramratan Sukal v. Nandw*³ where it was said : "It has now been conclusively settled that the third Court, which was in this case the Court of the Judicial Commissioner, cannot entertain an appeal upon any question as to the soundness of findings of fact by the second Court ; if there is evidence to be considered, the decision of the second Court, however unsatisfactory it might be if examined, must stand final" and observed at page 99 : "The present case does not come within that rule. The facts found need not be questioned. It is the soundness of the conclusions from them that is in question, and this is a matter of law." This is exactly the case here where the question for determination is the question of the status of an individual. Moreover when the Commissioner has committed so many errors of law and misunderstood the legal position which exists between the shareholders of a

(1) (1918) I.L.R. 46 Cal. 189.

(2) (1892) I.L.R. 20 Cal. 93.

(3) (1892) 19 I.A. 1.

company and the company itself, it is impossible to accept as correct the so called finding of fact arrived at by the Commissioner of Income-tax. I must hold in law that the assessee is possessed of the business and property in question as an individual.

I would, therefore, answer the first question in the affirmative and would give the answer to the second question in these words : " The income from business, property, etc., is assessable as the income of Sirdar Indra Singh alone and not as the income of the joint Hindu family."

It now remains to answer question No. 3. This concerns a sum of Rs. 12,000 which was received by the assessee as his remuneration as governing director under articles 111 and 116 of the articles of association of Indra Singh and Sons Limited, a private company. In the latter article it is distinctly stated that this sum is his personal remuneration. *Prima facie* it is his own individual income. Even if it is assumed that the shares which were held by Sirdar Indra Singh (the holding of at least 10,000 shares is a necessary qualification to become the governing director of the private company) belong to the joint family, the remuneration received by Sirdar Indra Singh cannot be held in law to be the remuneration of the joint Hindu family. The joint Hindu family would be entitled to the dividends earned upon the shares which they transferred to Sirdar Indra Singh in order to become the governing director. The Commissioner in my opinion was in error in treating this Rs. 12,000 as the income of the joint Hindu family. The Commissioner relies upon the fact that Sirdar Indra Singh in his return of income dated the 14th July, 1937, for the year 1937-38 declared the assessable income to be the aggregate of the director's fees of all the three members of the family, that is himself and his two sons. But in my opinion this declaration is of no consequence. As Sirdar Indra Singh was filing a return on behalf of the joint Hindu family he included all the income of the members but that would not make an individual income the income of the joint family as such.

For these reasons, I would answer question No. 3 in the negative, that is to say Rs. 12,000 cannot be included in the income of the Hindu undivided family.

In the view which I have taken it is unnecessary to consider the alternative argument advanced on behalf of the assessee by Mr. Isaacs. But it is proper that I should express my views on this aspect of the case also.

Section 25A, sub-clause (1), clearly provides that "where, at the time of making an assessment under Section 23, it is claimed by or on behalf of any member of a Hindu family hitherto assessed as undivided that a partition has taken place among the members of such family, the

Income-tax Officer shall make such enquiry thereinto as he may think fit, and, if he is satisfied that a separation of the members of the family has taken place and that the joint family property has been partitioned among the various members or groups of members in definite portions he shall record an order to that effect." By the third sub-clause it is provided that "where such an order has not been passed in respect of a Hindu family hitherto assessed as undivided, such family shall be deemed, for the purposes of the Act, to continue to be a Hindu undivided family." The argument of Mr. Isaacs was that by the transactions so often referred to above in 1935-36 there was a disruption in the family because by the division of Rs. 30,00,000 into three equal portions, a partition of the joint Hindu family property has been made in ascertaining the shares of the individual members, and that as in a Mitakshara family it is impossible to predicate the shares of the members of a joint Hindu family the result in law was that the family is no longer an undivided Hindu family. There is force in this contention. But even so the provisions of Section 25A, sub-clause (3), stand firmly in the way of the success of this argument. In this case such a claim was not made at the time of making the assessment under Section 23. The assessee did not put forward such a claim before the Income-tax Officer. It is true that the assessee would hesitate before putting forward such an alternative claim before the Income-tax Officer, but the provisions of Section 25A are quite clear. Such a claim has to be made at the time of making an assessment under Section 23. Further sub-clause (3) is equally clear that where the Income-tax Officer has not passed such an order then such family shall be deemed for the purposes of the Act to continue to be an undivided family so that even if the argument of Mr. Isaacs is accepted that such a family in law was not a Hindu undivided family in and after 1936, but for the purposes of the Income-tax Act it must be deemed to continue to be a Hindu undivided family. For these reasons the alternative argument of Mr. Isaacs is not sound and must be overruled.

The reference is accordingly answered as follows :—

Question No. 1.—Sirdar Indra Singh and his two sons constitute a Hindu undivided family for the purposes of the Indian Income-tax Act (XI of 1922).

Question No. 2.—The income from the business, property, etc., is not assessable as the income of the joint family but of Sirdar Indra Singh alone.

Question No. 3.—The income of Sirdar Indra Singh as managing director of Indra Singh and Sons Ltd., amounting to Rs. 12,000 in

the year of account cannot be included in the income of the Hindu undivided family.

As the whole of this dispute has arisen due to the different statements made by Sirdar Indra Singh deliberately before the Income-tax authorities, I would direct that each party should bear his own costs of this reference. The Commissioner of Income-tax will retain Rs. 100 which was deposited with him by the assessee under Section 86 of the Act.

HARRIS, C.J.—I entirely agree.

Reference answered accordingly.

[IN THE MADRAS HIGH COURT.]

PR. AL. M. MUTHUKARUPPAN CHETTIAR

v.

COMMISSIONER OF INCOME-TAX, MADRAS.

SIR LIONEL LEACH, C. J., and LAKSHMANA RAO, J.

October 19, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 10 (2) (ix), 24—
MONEY-LENDING BUSINESS—LARGE BUILDING TAKEN ON LEASE FOR
SUB-LETTING—COMPROMISE OF DISPUTE AS TO VALIDITY OF LEASE AND
SETTLEMENT OF CLAIMS AGAINST SUB-LESSEES AND CO-LESSEE—LOSS
INCURRED IN SETTLEMENT AND LITIGATION EXPENSES—WHETHER
ALLOWABLE AS TRADING LOSS OR BUSINESS EXPENDITURE.

The assessee firm carried on a money-lending business in Rangoon in partnership with the S.P.K.A. Firm under the vilasam S.P.K.A.A.M. Firm. The S.P.K.A.A.M. Firm and another firm entered into a lease of a large building in Rangoon and sub-let part of it to other Chettiars. Disputes as to the validity of the lease were settled by payment to the landlord of a sum of Rs. 1,98,650. In 1937 the assessee and the S.P.K.A. Firm filed a suit to recover a portion of this amount from the sub-lessees and their co-lessee, and in 1937-38 some of the claims were settled which resulted in a loss of Rs. 45,424. The assessee wrote off in his books the sum of Rs. 22,712 being half of the total loss and treated a sum of Rs. 1,335 spent in litigation as business expenditure. The Income-tax authorities disallowed both the claims :

Held, that the entering into a lease of a large building in Rangoon was entirely outside the assessee's business as a money-lender and therefore the loss suffered could not be treated as a business loss. The fact that the assessee chose to write off the amounts in the books kept by

him in connection with his money-lending business did not make any difference.

Case stated under Section 66 (3) of the Indian Income-tax Act (XI of 1922 before amendment) by the Commissioner of Income-tax, Madras, in pursuance of the High Court's judgment and order dated the 23rd February 1942: (O. P. No. 261 of 1941).

STATEMENT OF CASE.

"In accordance with the High Court's order quoted above, I have the honour to refer the following case for the decision of their Lordships under Section 66 (3) of the Indian Income-tax Act (XI of 1922 as it stood before Part II of the Act came into force), hereinafter referred to as the Act.

2. The petitioner who is an assessee on the file of the Income-tax Officer, Sivaganga circle, derives income from interest on securities, property, business in money-lending (headquarters Karaikudi, Rangoon and Singapore) and other sources (dividends and Burma income from agriculture). For the tax year 1938-39 'previous year', Tamil year Eswara ended 12-4-38 he was assessed by the Income-tax Officer, Sivaganga, on a total income of Rs. 68,410. In determining this income the Income-tax Officer disallowed *inter alia* a sum of Rs. 22,712 claimed as a loss arising from the lease of premises in Rangoon, and another sum of Rs. 1,335 being legal expenses incurred in connection therewith. The facts relating to these items are as follows:—

3. The S. P. K. A. A. M. Firm (consisting of the petitioner and one S. P. K. A. Firm as partners) and another firm known as O. N. R. M. M. Firm jointly obtained on lease under an agreement of lease dated 14th March 1929, a building in Mogul Street, Rangoon, on a rent of Rs. 3,000 per month for a period of years with a view to sub-let it to other Chettians operating in Mogul Street. There were in all 43½ box spaces in the premises taken on lease. The S. P. K. A. A. M. Firm took one box space and O. N. R. M. M. Firm another box space. The rest were allotted to the various other Chetty firms. An agreement was taken from the various Chetty firms in occupation of the premises whereby they agreed to be bound by the terms of the lease deed dated 14th March 1929 and to pay the proportionate rent and any charges and to reimburse and indemnify the lessees in respect of liabilities arising under the said lease. Subsequently the sub-lessees resiled from the scheme in whole or in part leaving liability for rent under the lease upon the lessees. In 1931 there were suits by the landlord against the lessees for recovery of rent and a counter suit by the lessees for a declaration of the invalidity of the lease deed. The disputes were finally settled in December 1934 by the Privy Council which decreed the landlord's suits and

dismissed the lessee's suit. Thereupon a compromise was entered into on 2nd January 1935. According to the compromise the lease was to be terminated by the payment of a sum of Rs. 1,98,650 by way of rent, compensation and damages. This amount was paid between January 1935 and June 1936. The amount paid was debited to a special folio opened in the name of No. 90 Mogul Street. About this time the S.P.K.A.A.M. became dissolved. Two separate firms were formed, each taking over one half of the assets of the S.P.K.A.A.M. Firm. These two firms were the Pr. Al. M. Firm (the petitioner) and the the S.P.K.A. Firm. Subsequently the petitioner and S.P.K.A. took steps to recover from the various sub-lessees the proportionate amounts payable by them and settled with some of them the claims against them.

4. In 1937 the petitioner and S. P. K. A. Firm filed a suit in the Rangoon High Court against some other sub-lessees and also against O. N. R. M. M., the co-lessee who was liable for one half of the lease amount under the original lease, but who seems to have become insolvent. In the year of account some of the defendants in the suits settled the claims against them. The amount waived in their favour on settlement was Rs. 45,424. One half of this, *viz.*, Rs. 22,712 was treated as petitioner's share and written off in the petitioner's books of the account year and claimed as a loss. In addition to this a further claim to deduct Rs. 1,335, being expenditure incurred in connection with the suits referred to above, was also preferred by the petitioner. The Income-tax Officer disallowed these claims on the ground that the sum of Rs. 1,98,650 paid to the landlord represented a payment by the S. P. K. A. A. M. Firm to get rid of an onerous contract or liquidated damages paid for breach of contract and that it was not a loan advanced in the course of the petitioner's business and written off as bad. He also held that the sum paid was not an expenditure incidental to the carrying on of the business or incurred for the earning of the profits. An extract of his order is filed marked exhibit A.

5. The petitioner appealed to the Appellate Assistant Commissioner. The Appellate Assistant Commissioner upheld the disallowance on the ground *inter alia* that,

(1) the lease in question was not a transaction in the course of the petitioner's business, as taking houses on lease and sub-letting them was not part of the petitioner's business and as there was no business element in the lease since the total rent payable for the entire premises was apportioned among the various occupants in equal shares,

(2) the payment to the landlord was one made as compensation for having terminated the lease which would otherwise have run up to 1939 and that the payment was similar to a payment to obtain a

contract which was held to be an inadmissible claim in the case of *Alagannan Chettiar v. Commissioner of Income-tax, Madras*¹,

(3) the amount paid under the terms of the compromise as a result of the Privy Council's decision could not be regarded as a payment for earning any income,

(4) the claim could not be regarded as a bad debt deductible from the business profits as the amount paid under the terms of the compromise could not be regarded as a loan advanced in the course of the business.

An extract of his order is filed marked exhibit B.

6. The petitioner thereupon applied to my predecessor under Section 66 (2) of the Act requesting him to refer to the High Court certain alleged questions of law arising out of the Appellate Assistant Commissioner's order. An extract of this application is filed marked exhibit C.

7. As my predecessor found that there was no question of law arising out of the Appellate Assistant Commissioner's order he declined to make a reference and dismissed the application. An extract of his order under Section 66 (2) is filed marked exhibit D.

8. On the application of the petitioner under Section 66 (3) of the Act the High Court has directed me to refer the following question and I accordingly refer it for the decision of their Lordships :—

“Whether the petitioner was not entitled on the facts and in the circumstances of the case to claim a deduction of Rs. 22,712 and Rs. 1,335 in the computation of the profits of his Rangoon business as allowable business loss or bad debts properly written off and whether the disallowance of the claim by the Income-tax authorities as capital loss not connected with the petitioner's money-lending business was legal or supported by any materials on record.”

9. The point in issue in this case was recently referred to the Rangoon High Court in a different form by the Commissioner of Income-tax, Rangoon, at the instance of the other partner of the defunct S.P.K.A.A.M. firm. The Rangoon High Court held that “the loss sustained was not one incurred as a trading loss in the year under assessment, but was a capital loss.” In view of this I have not considered it necessary to discuss the point in detail. I would, however, add that the disallowance of the sum of Rs. 22,712 is also supported by the decision in *Chimanlal Rameshwarlal v. Commissioner of Income-tax, Bengal*², *Commissioner of Income-tax, Burma v. S. P. K. A. R. M. Family*³, *Rm. Ar. Ar. Rm. Arunachalam Chettiar v. Commissioner of Income-tax, Madras*⁴ and *Alagannan Chettiar v. Commissioner of*

(1) (1927) 3 I.T.C. 44.

(2) (1940) 8 I.T.R. 408.

(3) (1941) 9 I.T.R. 685.

(4) (1936) 4 I.T.R. 173; 9 I.T.C. 282.

*Income-tax, Madras*¹. The sum of Rs. 1,335 which represents legal expenses incurred in connection with the suits for the recovery of the sums due by the sub-lessees of the defunct firm stands on the same footing and is also of a capital nature. It is submitted that the answer to the reference should be that the petitioner is not entitled to the deduction claimed by him."

K. V. Sesha Aiyangar, for the Commissioner.

P. R. Srinivasan, for the assessee.

JUDGMENT.

(Judgment of the Court was delivered by the Honourable the Chief Justice).

The assessee carried on a money-lending business in Rangoon in partnership with the S.P.K.A. firm. The firm composed of the assessee and the S.P.K.A. firm was known as the S.P.K.A.A.M. firm. On the 14th March 1929, the S.P.K.A.A.M. firm and another Chettiar firm carrying on business in Rangoon, styled the O.N.R.M.M. firm, entered into a lease of a building in Mogul Street, Rangoon, at a rent of Rs. 3,000 per month. Chettians carrying on business in Rangoon all had their offices in Mogul Street. The lessees did not require the whole of the premises for their respective businesses and their intention was to sub-let parts of the building to other Chettians. This they did, but the sub-lessees did not pay in full what was due from them by way of rent. The lessees themselves disputed the validity of the lease with their landlord and the case was carried to the Privy Council. The Privy Council held that the lease was valid and therefore the lessees were responsible for the rent.

On the 2nd January 1935, after the Judicial Committee had given its decision, the lessees entered into a compromise with their landlord under which the remainder of the term of the lease was to be cancelled and the lessees were to pay to him the sum of Rs. 1,98,650 by way of rent, compensation and damages. Each of the sub-lessees had agreed to pay a proportion of the rent and to reimburse and indemnify the lessees in respect of any liability arising under the lease. The S.P.K.A.A.M. firm paid the landlord the Rs. 1,98,650 between January 1935 and June 1936 and then dissolved.

In 1937 the assessee and the S.P.K.A. firm filed a suit in the Rangoon High Court against the sub-lessees and their co-lessee, the O.N.R.M.M. firm, to recover their proportions of the Rs. 1,98,650. The O.N.R.M.M. firm was in fact liable to the extent of one half. In the

year of account (1937-38) the plaintiffs settled with some of the defendants and the settlements resulted in a loss of Rs. 45,424. The loss was apportioned between the S.P.K.A. firm and the assessee, and the assessee wrote off in his books the sum of Rs. 22,712 being half of the total loss. In addition he treated the sum of Rs. 1,335 spent in the litigation as business expenses.

The Income-tax authorities refused to recognize these sums as being legitimate deductions in calculating the amount of profits for that year. The assessee objected and asked the Commissioner of Income-tax to state a case. He refused to do so, but was directed by this Court to make this reference under Section 66 (3) of the Indian Income-tax Act. The question referred reads as follows:—

“Whether the petitioner was not entitled on the facts and in the circumstances of the case to claim a deduction of Rs. 22,712 and Rs. 1,335 in the computation of the profits of his Rangoon business as allowable business loss or bad debts properly written off and whether the disallowance of the claim by the Income-tax authorities as capital loss not connected with the petitioner's money-lending business was legal or supported by any materials on record.”

The case has now been fully argued and we are of the opinion that the question should be answered against the assessee. The entering into a lease of a large building in Mogul Street was no part of the assessee's business as a money-lender. He and his partner entered into the lease in the hope that they would be able to recover from their sub-lessees most of the rent to be paid to the landlord. This was a transaction which was entirely outside the business of money-lending and this being the case the loss suffered could not be treated as a business loss. As it was not a business loss it could only be regarded as a capital loss. The fact that the assessee chose to write off the amount in the books kept by him in connection with his money-lending business does not make any difference.

The question referred will be answered accordingly. The assessee must pay the costs, Rs. 250.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]
MESSRS. CHIMANRAM MOTILAL
v.

COMMISSIONER OF INCOME-TAX, (CENTRAL), BOMBAY.

BEAUMONT, C. J., and KANIA, J.

September 22, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE AMENDMENT OF 1939), SEC. 34—RE-ASSESSMENT—INCOME ESCAPING ASSESSMENT—NOTICE—SOURCE OF ESCAPED INCOME—WHETHER SHOULD BE SPECIFIED—WRONG ALLOWANCE OF LOSS—WHETHER INCOME ESCAPED ASSESSMENT—BURDEN OF PROOF—RE-ASSESSMENT BASED ON LESS MATERIAL—VALIDITY.

Where a notice under Section 34 of the Income-tax Act was issued to an assessee who had only one source of income, stating that the Income-tax Officer had reason to believe that the assessee's income from all sources which arose, accrued or was received in the previous year had partially escaped assessment :

Held, that the notice was valid and the failure to specify the particular source of income that had escaped assessment did not render it invalid. All that is necessary under Section 34 is that a notice should be given which sufficiently draws the attention of the assessee to the case which he has to meet.

Under Section 34 of the Act an Income-tax Officer or his successor is entitled to re-assess an income on the ground that owing to some mistake in the first assessment income has escaped assessment. The power to re-assess is not confined to cases where some fresh facts are brought to the notice of the Income-tax Officer or there is a change in the law. But income cannot be held to have escaped assessment merely on the ipse dixit of the Income-tax Officer. It is for him to establish to his own satisfaction on the assessment, and subsequently before any Appellate Tribunal, that income has escaped assessment ; it is not for the assessee to prove that the original assessment was right and that no income has escaped assessment.

The assessee who was doing business in silver and also straddle business was allowed by the Income-tax Officer to set off against the business profits of S. 1991-92 a sum of Rs. 3 lakhs being the loss on account of straddle transactions entered in the books of S. 1990-91. Subsequently in 1938 the same officer came to the conclusion that the loss of Rs. 3 lakhs was not incurred in the year S. 1991-92 and could not be allowed under Section 24 and he therefore issued a notice under Section 34 alleging that the amount allowed as a deduction had escaped assessment. Without seeing the books of S. 1990-91, which were

not then available, and without any additional or new evidence the Income-tax authorities held in 1940 that the straddle transactions were not proved and therefore the sum of Rs. 3 lakhs had escaped assessment :

Held, that although the notice under Section 34 was justified, there was no evidence on which the Income-tax authorities could come to the conclusion that any income had escaped assessment.

Per KANIA, J.—The question of law about the application of Section 34 could only arise if on the same materials at least the second officer had come to a different conclusion.

Commissioner of Income-tax, Burma v. U Lu Nyo [1938] (1 I.T.R. 373) and *Commissioner of Income-tax v. Dey Brothers* [1936] (4 I.T.R. 209) commented upon.

Cases referred to :—

Amir Singh Sher Singh v. Commissioner of Income-tax (1935) 3 I.T.R. 171.

Anglo Persian Oil Company Ltd. v. Commissioner of Income-tax (1933) 1 I.T.R. 129 ; 60 Cal. 840 ; 37 C.W.N. 430 ; A.I.R. 1933 Cal. 777 ; 6 I.T.C. 419.

Commissioner of Income-tax v. Dey Brothers (1936) 4 I.T.R. 209 ; 9 I.T.C. 313.

Commissioner of Income-tax, Bengal v. Mahaliram Ramjidas (1940) 8 I.T.R. 442 ; 44 C.W.N. 929 ; A.I.R. 1940 P.C. 124.

Commissioner of Income-tax, Bombay v. Manohar (1935) 3 I.T.R. 372 ; 59 Bom. 626.

Commissioner of Income-tax v. D. R. Naik (1939) 7 I.T.R. 362 ; 1939 Bom. 445 ; 41 Bom. L.R. 652 ; A.I.R. 1939 Bom. 362.

Commissioner of Income-tax, Bombay v. P. N. Contractor (1937) 5 I.T.R. 338 ; I.L.R. 1937 Bom. 310 ; 169 I.C. 376 ; 39 Bom. L.R. 123 ; A.I.R. 1937 Bom. 214.

Commissioner of Income-tax v. Rajah of Parlakimedi (1925) I.L.R. 49 Mad. 22 ; 91 I.C. 940 ; 2 I.T.C. 104.

Commissioner of Income-tax, Burma v. U Lu Nyo (1933) 1 I.T.R. 373 ; 146 I.C. 300 ; A.I.R. 1933 Rang. 350 ; 7 I.T.C. 47 ; 12 Rang. 118.

Madan Mohan Lal v. Commissioner of Income-tax (1935) 3 I.T.R. 438 ; 16 Lah. 937 ; 158 I.C. 718 ; A.I.R. 1935 Lah. 742 ; 8 I.T.C. 413.

P. C. Mallick and D. C. Aich, In re (1940) 8 I.T.R. 236.

Rajendranath Mukherji v. Commissioner of Income-tax, Bengal (1934) 2 I.T.R. 71 ; 61 Cal. 285 ; 38 C.W.N. 319 ; 66 M.L.J. 121 ; 147 I.C. 663 ; A.I.R. 1934 P.C. 30 ; 36 Bom. L.R. 267 ; 7 I.T.C. 143.

Case referred to the High Court by the Income-tax Appellate Tribunal (Bombay Branch) under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by Section 92 of the Indian Income-tax (Amendment) Act (VII of 1939) for the decision of the following questions of law :—

(1) Whether in the circumstances of this case the notice of re-assessment issued to the applicant under Section 34 of the Income-tax Act was invalid or illegal for failure to specify the particular source of income that had escaped assessment?

(2) Whether in the circumstances of the case a part of the applicant's income had escaped assessment within the meaning of Section 34 of the Indian Income-tax Act, so that it could be re-assessed by the second Income-tax Officer.

Income-tax Reference No. 3 of 1942. The facts of the case appear in the judgment of the Appellate Tribunal and in the Statement of Case.

JUDGMENT OF APPELLATE TRIBUNAL.

Under Section 33 of the Indian Income-tax Act (XI of 1922) the Income-tax Appellate Tribunal, (Bombay Branch) (consisting of N. R. GUNDIL, Judicial Member, and P. C. MALHOTRA, Accountant Member) delivered the following judgment on 10th May 1941.

“ This appeal calls into question a supplementary assessment made by the Income-tax Officer, under Section 34 of the Income tax Act and confirmed by the Appellate Assistant Commissioner of Income-tax, A Range, Bombay, on 9th December 1940.

2. The contest is in regard to the assessment made in the assessment year 1936-37. The original assessment for the year in question was made by the Income-tax Officer on 9th July 1937 computing the appellant's assessable income at Rs. 1,47,160. Some time later, on definite information received, the same Income-tax Officer issued a notice under Section 34 to the appellant to make a fresh return of his income, stating that his income from “all sources” had partially escaped assessment. The matter came before another Income-tax Officer who on 23rd July 1940, made a fresh assessment, computing the assessable income at Rs. 4,54,417. The appellant asks that this latter assessment be set aside on three main grounds, which we will consider in order.

3. In the first place, it is contended that the notice under Section 34 was irregular and invalid, because no particular source of income was shown in the notice as having escaped assessment. The learned counsel pointed out a form of the notice prescribed at page 269 of the *Income-tax Manual*, 7th Edition, and contended that the Income-tax Officer was bound to abide by the particular form. The present case is governed by Section 34 as it stood before the amendment of 1939. A form of notice under that section is prescribed in the *Income-tax Manual*, and one of the two footnotes referring to the mode of filling in the blank space in the body of the notice is worded “ Here enter the source.” No such footnote, however, occurs in the form in 8th Edition of the *Income-tax Manual* compiled after the Income-tax Act was amended in 1939. The learned departmental representative, however, maintained that Section 34 itself did not prescribe a notice in any particular form, and that the departmental instructions contained in the *Income-tax Manual* were intended only as directory and not by any means mandatory. He urged further that even if the Income-tax Officer had written a letter that would have been a sufficient compliance with law, provided it stated that an assessee's income or part of his income had escaped assessment. Without going as far as to

accept the latter proposition, it appears to us to be clear that all that Section 34 requires is a notice containing all or any of the requirements which may be included in a notice under Section 22 (2) of the Act. This view is supported by *In the matter of Messrs. Burn & Co.*¹ followed in *Jawala Prasad Chobey v. Commissioner of Income-tax, Bengal*². Moreover, in the present case, the appellant had no different sources of income. His only source was business. Thus the expression "all sources" occurring in the notice really meant one source, that is to say, the appellant's business. That being so, we do not think that the appellant could be unaware of the source which was stated to have escaped assessment and which was intended to be re-assessed. At any rate, the appellant put in a return in compliance with the notice and might be therefore taken to have waived the irregularity, if any. We are therefore unable to hold that the notice was bad in law.

4. The most important dispute in this appeal has reference to the re-assessment of three items, namely, Rs. 2,95,619, Rs. 8,368 and Rs. 3,000. The first is alleged to be a loss arising out of connected transactions of straddle business done by the appellant in Samvat 1990-91, and carried forward to the accounting year Samvat 1991-92. The second item is an aggregate of different sums lying to the credit of several individuals who are alleged by the respondent to be fictitious. The third item of Rs. 3,000 is alleged to be the amount paid by the appellant as rebate from exchange brokers, and not accounted for in his books.

(a) The sum of Rs. 2,95,619 is the opening debit balance in the Vilayat Badla account brought forward from the books of Samvat 1990-91, and represents the figure of losses incurred in silver speculation *in India* in the months of Shrawan, Bhadarva and also of Samvat 1990-91. The bringing forward of the losses into the accounts of subsequent years was contrary to Section 24 of the Income-tax Act as it stood before its amendment by the additions of several provisos in 1939. In other words, an assessee was not entitled to any allowance in this respect so as to set off the losses thus brought forward to the profits of the next year. The learned counsel for the appellant, however, contended that the several transactions resulting in loss were a part of the straddle transactions done by the appellant in London, it would not be a correct thing to include the items of the loss in the profit and loss account of the Samvat 1990-91, as the connected transactions were done in England, and the profit amounting to Rs. 1,96,000 and odd has been brought in in the books of account for

(1) (1934) 2 I.T.R. 30.

(2) (1935) 3 I.T.R. 295.

the year Samvat 1991-92; and that therefore this loss was really not for the Samvat 1990-91 but for 1991-92. The learned departmental representative, however, maintained that the appellant did not produce the books for the year Samvat 1990-91 at the time of the reassessment, nor produced them even at the time of the original assessment, and that therefore it was not established that any straddle business was done by the appellant as alleged by him. We are not quite sure about the correctness of the second part of the learned departmental representative's statement, i.e., regarding the non-production of the books at the time of the original assessment. The record contains the Examiner's report of the original assessment. It shows the details of the item of Rs. 2,95,619, which, in our opinion, was not possible to ascertain unless the books of Samvat 1990-91 were before the Examiner. However, the point has no material bearing on the question before us and need not be noticed further. The fact remains that we have little or no evidence of any straddle business done by the appellant in London in the year in question. Assuming, however, that he did such kind of business in London, it will have to be borne in mind that the loss with which we are concerned in this case had been incurred in respect of Bombay transactions, and had been ascertained before the end of the year, or, at any rate, before closing the accounts for that year. The transactions done in London could not in any sense be regarded as any part of the corresponding transactions made in India. Obviously, the London transactions must have been made as a cover for any possible losses here. In other words, the two sets of transactions were, in our opinion, altogether independent. We therefore fail to find any justification for the item of Rs. 2,95,619 not being adjusted in the profit and loss account of the year in which they were sustained. Next, the method of accounting adopted by the appellant has been to bring in the losses or profits in Bombay transactions in the particular financial year in which the settlements were made; and the losses and profits of England in the particular financial year in which the advices were received from England. It is, however, remarkable that in the years under assessment he has maintained the same method as adopted by him all through in the case of Vilayat Badla account, but has varied it in the case of Bombay transactions which he could not do. It was a variation in the method of accounting regularly employed by the assessee. It is admitted that the appellant has been continuously adopting the method as just stated. This part of the case may be summarised as follows. In the assessment year 1935-36, the appellant did not include the losses suffered by him for the months of Shrawan, Bhadarya and Aso, i.e., he

brought in the transactions of 9 months only for the Bombay transactions. But in the case of London transactions he followed his usual practice of bringing in the loss and profit of 12 months. In the assessment year 1936-37, however, he brought in his profit for the Vilayat Badla account (London transactions) for the period of 12 months as had been done by him all through in the previous year and also subsequent years; but in the case of the Bombay transactions he brought in profit and loss for 15 months which he could not do under the Act. In order to find out the assessable income for the assessment year 1936-37, only 12 months' transactions should have been included as far as Bombay transactions were concerned, and not 15 months' as was done by the appellant. His object in adopting the particular course that he did appears to us to be transparent enough. For the assessment year 1935-36 the appellant was assessed on a total income of Rs. 12,879 only. This income being divided among a number of partners, no tax could be levied from the appellant in that year. If the loss of Rs. 2,95,619 had been brought in the computation, as it should have been done, it would have made practically no difference to the appellant's liability to the payment of the tax (*sic*) was concerned. He must have found that he had made large profits in the assessment year 1936-37 when he put in his return for 1935-36, on 6th June 1935. Accordingly, he cleverly manipulated his accounts by not bringing this item to the debit of his profit and loss account of 1935-36, but resorted to the device of carrying it forward the next year with a view to evade income-tax on the profits accrued during the assessment year 1936-37. Apparently, the Income-tax Officer who made the first assessment was not able to detect the appellant's underlying motive at that time, and so soon as he realised the effect of such an entry he forthwith served the appellant with a notice under Section 34. For these reasons, we are unable to hold that this item of loss should not be excluded from the assessment of the year under reference.

(b) Taking up the second item of Rs. 8,368 it is an aggregate of 5 items in a corresponding number of personal accounts. The appellant has a large number of such accounts. The Income-tax Officer required the appellant to prove that the 5 items were actually due by the appellant to the persons to whose credits they are lying. He appears to have thought that the parties were fictitious. The appellant wrote a letter to the Income-tax Officer giving the names and addresses of the persons to whom these amounts were due. The learned counsel for the appellant has urged that it was not possible for him to actually produce these parties before the Income-tax Officer, and it was the duty of the

latter to make necessary inquiries regarding the persons to whom the amounts were shown to be due in the appellant's books. The appellant was actually able to produce the parties in some cases, and the Income-tax Officer allowed those sums. In a big concern like that of the appellant where there are a large number of personal accounts we think that it was a hardship if a production of every creditor was insisted upon. Beyond the bare fact that the appellant was not able to produce these 5 persons, we do not find anything to sustain the Income-tax Officer's view more especially having regard to one of his remarks contained in his report dated 8th July 1940 to the Appellate Assistant Commissioner, Central, Bombay. He told the latter that the examination of accounts over again did not disclose any suspicious facts. We think therefore that the sum of Rs. 8,868 was an aggregate of 5 different sums due by the appellant to the respective persons whose names and addresses were given by the appellant, and that it did not form a part of his income.

(c) The contest in regard to the last item of Rs. 3,000 has no substance whatsoever. Admittedly, this sum was not brought in in the appellant's books. It was said that it really belonged to several sub-brokers. We think that it was the duty of the appellant to show the receipt of this sum as his income and claim a deduction for the payment alleged to have been made to the sub-brokers. In our opinion, his failure to do so justified the Income-tax Officer in adding back this item in the appellant's assessment for the year under reference.

5. The last point taken by the appellant's learned counsel is that the re-assessment under Section 34 was illegal as it was not proved that any income had escaped assessment at the time when it was originally made. From the facts stated before, it must be perfectly clear that the original assessment was wrong as the Income-tax Officer had taken into account the Bombay transactions of 15 months instead of 12 months; and secondly, because the sum of Rs. 3,000 had been received by the appellant as income and not accounted for in his books. The learned counsel relies upon the case of the *Commissioner of Income-tax, Bombay v. Gopal Vairnath*¹. But far from supporting the appellant it appears to be reinforcing the view that we take of the case. The actual decision of the case depended upon its particular facts; but the observations of Beaumont, C.J., and Rangnekar, J., are clearly to the effect that Section 34 should not be confined to cases in which a source has escaped assessment, but that its provisions extend to correcting an assessment in which a deduction had been improperly allowed. Their Lordships expressed themselves in full agreement with the remarks by

Rankin, C.J., in the *Anglo Persian-Oil Company (India) Ltd. v. The Commissioner of Income-tax*¹, which are to the effect that the Income-tax authorities can put right an assessment by which a deduction has been improperly allowed. That is exactly the case here. The Income-tax Officer who first made the assessment committed an error of judgment which amounted to a mistake of law by allowing a deduction of Rs. 2,95,619 from the assessable income of the appellant who had brought in 15 months' transactions instead of 12 months' in the computation. In other words, it was an improper deduction which could, in our opinion, be set right under Section 34. We, therefore, hold that he was fully justified in assessing the appellant under Section 34 of the Indian Income-tax Act.

6. The result is that we partially allow this appeal, and order that the sum of Rs. 8,368 be allowed to the appellant, and deduct it from the total assessable income for the year under reference. The rest of the appeal is dismissed."

On the application of the assessee under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by Section 92 of the Indian Income-tax (Amendment) Act (VII of 1939) the Appellate Tribunal referred the case to the Bombay High Court:—

STATEMENT OF CASE.

"This is an application by the assessee firm of Messrs. Chimanram Motilal (Gold & Silver), under Section 66 (1) of the Income-tax Act, requiring us to refer to the Hon'ble High Court of Bombay three questions of law stated to be arising out of our order, dated May 10, 1941, under sub-section (4) of Section 88 of the Act, in Regular Assessment Appeal No. 4 (Bombay) of 1940-41. Before setting out these questions and the reply which the respondent has filed under Rule 54 of the Appellate Tribunal Rules, we shall briefly state the case as below:—

2. The applicant was assessed on a total income of Rs. 1,47,160 for the assessment year 1936-37, the relevant accounting year being Maru year 1991-92. The order of the Income-tax Officer, Special Circle, Bombay, dated 9th July, 1937, in this connection is marked Ex. "A" in the list of documents appended to this reference.

3. On information received some time later that applicant's profits had partially escaped assessment, the same Income-tax Officer issued a notice, dated 22nd March, 1936, under Section 34 of the Indian Income-tax Act, 1922, calling upon him to make a fresh return of his income for the assessment year in question. The section came to be amended

in 1939 ; but the section as it stood before amendment is appropriate to this case. It is stated in the notice that the applicant's income from "all sources" had partially escaped assessment and that it was therefore proposed to assess the said escaped income. The notice is marked Ex. "B".

4. In response to the notice the applicant made a return declaring an income of Rs. 1,47,160 which was the amount originally assessed by the Income-tax Officer on 9th July 1937, as stated before. The return is marked Ex. "C".

5. The re-assessment proceedings were thereafter taken up by the Income-tax Officer, Section VII (Central), Bombay, who in course of his examination of the applicant's accounts discovered three items which, he thought, had escaped assessment in the year in question. These three items, respectively, are Rs. 2,95,619, Rs. 8,638 and Rs. 3,000. Accordingly he added back these amounts to the applicant's income as originally computed, and made a re-assessment on a total income of Rs. 4,54,417. The Income-tax Officer's order, dated July 23, 1940, is marked Ex. "C".

6. The first item of Rs. 2,95,619 represented the applicant's losses in Indian silver speculation which they had successfully claimed to set off against the profits of the accounting year, *i.e.*, Maru year 1991-92, thus reducing the total income of the year to that extent. The second item of Rs. 8,638 was an aggregate of sums lying to the credit of personal accounts of five persons; and the third item of Rs. 3,000 was stated to be payments made to sub-brokers.

7. The Income-tax Officer's reasons for adding back these sums to the applicant's income may be briefly stated. He thought that the loss of Rs. 2,95,619 had been incurred by the applicant in silver speculation in India in the Maru year 1990-91, *i.e.*, the year preceding the accounting year under reference, and had been brought forward to the accounting year Maru 1991-92 contrary to the provisions of Section 24 of the Indian Income-tax Act which, as it then stood, did not permit such a course. He therefore held that this loss was erroneously permitted to be set off against the profits of the accounting year, and that the profits reduced to that extent should be added to the applicant's income. As regards the second item of Rs. 8,638, the Income-tax Officer thought that the persons to whose accounts the sums were credited were really nominees of the applicant and that it really represented the applicant's own profits. The third and the last item of Rs. 3,000 was the profit actually received by the applicant, but which was not accounted for in the books on the ground that it was paid to sub-brokers by way of rebate. The Income-tax Officer held that there was no proof of this payment.

8. From this order of the Income-tax Officer, the applicant appealed to the Appellate Assistant Commissioner, A-Range, Bombay, who confirmed the assessment. A copy of his order is marked Ex. "D".

9. An appeal [R. A. A. No. 4 (Bombay) of 1940-41] was filed in the Appellate Tribunal from the order of the Appellate Assistant Commissioner. It was heard and disposed of by us on May 10th, 1941. A copy of the grounds of appeal to the Tribunal is marked Ex. "E" and that of our order in appeal is marked Ex. "F".*

10. We partially accepted the appeal, by excluding the second item of Rs. 8,638 from the income holding that the sums composing it were due to respective persons to whose accounts they had been credited, and that therefore these sums could not be regarded as a part of the applicant's income. The reasons for our finding will be found in para. 4 (b) of our judgment.

11. We rejected the rest of the appeal. As regards the amount of Rs. 3,000, we held that the applicant's failure to bring this sum into their accounts justified the Income-tax Officer's conclusion. Our reasons on the point are contained in para. 4 (c) of the judgment.

12. The main contest before us and which occasions the present reference, was focussed on the addition of the first item of Rs. 2,95,619. On the question of fact we found that the amount was the loss which the applicant had suffered in silver speculation made in India in the Maru year 1990-91, and brought forward to the accounting year Maru 1991-92. In view of this finding of fact, we held that the loss could not be set off against the profits of the accounting year having regard to the old Section 24 of the Act which applied to the case and which did not permit bringing forward of loss in a case like this. We have dealt with this part of the case in para. 4 (a) of our judgment.

13. In the application for reference under Section 66 (1) of the Income-tax Act, marked Ex. "G", the applicant has formulated the following three questions of law as arising out of our appellate judgment:—

"(1) Whether the notice under Section 34 is valid in law.

(2) Whether in the circumstances of the case a part of the income of the previous year had "escaped assessment" within the meaning of Section 34.

(3) Whether the proceedings taken under Section 34 in this case are valid in law."

14. In his written reply, marked Ex. "H", the respondent substantially concedes that the first two questions do arise out of our appellate judgment. As regards the third, his contention is that it is either a repetition of question No. 1 or No. 2, and that in either case it

*The Judgment of the Appellate Tribunal is printed at p. 46 *supra*,

is redundant. The learned Attorney for the applicant has explained that the third question implies that the re-assessment of the applicant was invalid, either because the initiation of the proceedings under Section 34 of the Income-tax Act was contrary to law on account of the defect in the notice itself, or, because the re-assessment amounted to a revision of an assessment by the second Income-tax Officer sitting in judgment over the first. But we think that such a result will follow from the answers to the first two questions which we shall endeavour to frame in more correct form.

15. One of the contents of the notice, Ex. "B", given to the applicant raises the first question. A form of notice that an Income-tax Officer is instructed to issue under Section 34 is printed at para. 105 of the *Income-tax Manual*, 7th Edition (1937). The first of the two footnotes to the form, which is deleted in the revised compilation of 1938 (8th Edition), required the Income-tax Officer to specify the source of the income that had escaped assessment in the blank space assigned for the purpose. In the present case, the Income-tax Officer filled in the blank space by writing "all sources". Thus the notice reads that the appellant's income from all sources had partially escaped assessment in the assessment year in question. It was contended before us that the notice was vague inasmuch as it omitted to specify the particular source of income that was stated to have escaped assessment; and that, therefore, it was irregular and invalid contravening as it did the express direction contained in the first footnote just referred to. We were unable to accept this contention, and our reasons will be found in para. 3 of our judgment. Briefly speaking, we held that Section 34 did not prescribe a notice in any particular form, except such notice containing all or any of the requirements which may be included in a notice under Section 22 (2) of the Act; and that the executive instructions contained in the *Income-tax Manual* could only be regarded as directory and not mandatory. So that a failure to strictly comply with the direction contained in the footnote did not vitiate the notice in question. We also held that since the only source of the appellant's income was business, the expression "all sources" occurring in the notice really meant but one source, *i.e.*, business: and that, that being so, the applicant could not have been left in doubt as to what source was meant by the notice in question. We further observed that the applicant must have known what the notice really meant, inasmuch as he made a return of his income as required by it. In this connection, we cited *In the matter of Messrs. Burn & Co.*¹, and *Jawala Prasad Chobey v. Commissioner of Income-tax, Bengal*². The respondent has cited a third

(1) (1934) 2 I.T.R. 30.

(2) (1935) 3 I.T.R. 295.

case of *Gopaldas Parshottamdas v. Commissioner of Income-tax, C. P. and U.P.*¹ in the present proceedings. The observations of their Lordships of the Allahabad High Court at page 135 of the report appear to further support the view that we took of the point.

16. Coming to the second question, it was contended before us that the amount of Rs. 2,95,619 could not be deemed to have "escaped assessment" inasmuch as the Income-tax Officer who had made the original assessment for 1936-37 had noted the items from the books of Maru 1990-91 and permitted the applicant to set off the loss against the profits of the relevant accounting year. On the other hand, it was contended for the Department that the applicant's books for that year were not produced before the Income-tax Officer, and that therefore he might have been misled into thinking that the loss in question had been really incurred in the accounting year itself. But we were unable to accept the Department's contention and substantially held that the books of 1990-91 must have been produced before the Income-tax Officer, and that the items in question did pass under his review. Thus the question before us resolved into whether, in the absence of any additional fact or evidence, the second Income-tax Officer who made the re-assessment had power to correct the assessment of the first Income-tax Officer who had, as a matter of fact, erroneously allowed the loss of Rs. 2,95,619 in the first assessment. In support of his contention the learned Attorney on behalf of the appellant relied upon the case of *Commissioner of Income-tax, Bombay v. Gopal Vajrath*². On the other hand, the Department cited the case of *Anglo Persian Oil Company (India), Limited v. Commissioner of Income-tax*³. The actual decision of the first case depended on its particular facts. But the observations of Beaumont, C. J., and Rangnekar, J., supported the view taken in the *Anglo-Persian Oil Company's case* that Section 34 of the Act should not be confined to cases in which a source has escaped assessment, but that its provisions extend to correcting an assessment in which a deduction had been improperly allowed. In this view that we took of the law, we hold that the re-assessment was properly made. Our reasons are stated in para. 5 of our judgment.

17. We, therefore, respectfully submit the following two questions to their Lordships:—

Questions referred

- (1) Whether in the circumstances of this case the notice of re-assessment issued to the applicant under Section 34 of the Income-tax Act was invalid or illegal for failure to specify the particular source of income that had escaped assessment?

(1) (1941) 9 I.T.R. 130.

(2) (1935) 3 I.T.R. 372.

(3) (1933) 1 I.T.R. 129.

- (2) Whether in the circumstances of the case a part of the applicant's income had escaped assessment within the meaning of Section 34 of the Indian Income-tax Act, so that it could be re-assessed by the second Income-tax Officer ?

18. These two questions are agreed to by the parties and are subject to the statement of the case given above."

Sir J. B. Kanga with *R. J. Colah*, for the assessee.

M. C. Setalvad with *G. N. Joshi*, for the Commissioner.

JUDGMENT.

BEAUMONT, C. J.—This is a reference made by the Income-tax Appellate Tribunal, (Bombay Branch) under Section 66 of the Income-tax Act, and it raises two questions relating to a further assessment made on the assessee under Section 34 of the Income-tax Act.

The first question which presents no difficulty whatever is:

"Whether in the circumstances of this case the notice of re-assessment issued to the applicant under Section 34 of the Income-tax Act was invalid or illegal for failure to specify the particular source of income that had escaped assessment?"

The notice under Section 34 stated that the Income-tax Officer had reason to believe that the assessee's income from all sources which arose, accrued or was received in the previous year had partially escaped assessment. It is said that the notice ought to have specified the particular source of income which was alleged to have escaped assessment, and reliance is placed on the form of notice given in the *Income-tax Manual*, which does state the source of the income which is alleged to have escaped assessment. But that form is not statutory. All that is necessary under Section 34 is that a notice should be given which sufficiently draws the attention of the assessee to the case which he has to meet, and as, admittedly, the assessee in this case has only one source of income, namely business, it seems to me plain that a notice saying that income from all sources had escaped assessment was quite sufficient to show them what the case was which they had to meet, namely, that some of their income from the only source from which any income was derived had escaped assessment.

The first question will therefore be answered by saying that the notice was valid.

The second question is: "Whether in the circumstances of the case a part of the applicant's income had escaped assessment within the meaning of Section 34 of the Indian Income-tax Act, so that it could be re-assessed by the second Income-tax Officer?"

The year of assessment is 1936-37, which is the Maru year 1991-92. In the original assessment the Income-tax Officer allowed under Section 24 of the Act as a deduction from the profits of the accounting year a sum of about Rs. 3 lacs, being the loss which the assessee had sustained in relation to the business in the year 1990-91. He considered that the loss in question could be brought into the accounts for the year of assessment 1991-92, because the business done in Bombay and the business done in London were what is called straddle business, and he held that the accounts had not been closed at the end of the year 1990-91. Subsequently, the same Income-tax Officer came to the conclusion that he had made a mistake, that he ought to have held that the loss of Rs. 3 lacs was not incurred in the Maru year 1991-92, and could not be allowed under Section 24 and he, therefore, gave a notice under Section 34 alleging that the amount allowed as deduction had escaped assessment. The actual hearing of the notice of re-assessment was carried out by another Income-tax Officer, who agreed that the sum of about Rs. 3 lacs ought not to have been allowed as a deduction and that the sum had escaped assessment.

Section 34 of the Act before the amendments of 1939 provided that if for any reason income, profits or gains chargeable to income-tax had escaped assessment in any year or had been assessed at too low a rate, the Income-tax Officer might, at any time within one year of the end of that year, serve a notice, and then proceed to re-assess by the method laid down under the Act for the original assessment.

It is argued by the assessee that it cannot be said that income has escaped assessment, unless there have been some additional facts brought to the notice of the Income-tax Officer, or some change in the law effected or revealed since the original assessment; and that if the Income-tax Officer merely changes his opinion, or if a fresh Income-tax Officer merely disagrees with the opinion of a previous Income-tax Officer, and therefore includes further income in the assessment, it cannot be said that any income has escaped assessment.

The view which was taken by the Rangoon High Court in *Commissioner of Income-tax, Burma v. U. Lu Nyo*¹ was that if once a source of income had been assessed, the matter was disposed of, and it could not be said that any income from that source had escaped assessment. But that view, which was not necessary for the actual decision of the particular case, which dealt with a difference of opinion between two Income-tax Officers on a mere matter of estimate, has not found favour with any other High Court in India. This Court differed from that view in *Commissioner of Income-tax, Bombay v. Manohar*², although we

(1) (1933) 1 I.T.R. 373

(2) (1935) 3 I.T.R. 372.

agreed with the actual decision and followed it in that case which was also a case in which one Income-tax Officer had differed from an estimate formed by a previous Income-tax Officer. The Rangoon High Court in a later case, *Commissioner of Income-tax v. Dey Brothers*¹, adhered to its former opinion but, as I have said, no other High Court has accepted that view.

The other High Courts have taken the view that the only question under Section 34 is whether in fact income has escaped assessment, and that income which might have been, but was not assessed, has escaped assessment and one ground on which income may undoubtedly be shown to have escaped assessment, is that the true facts were not brought to the notice of the Income-tax Officer. But if one admits that in such a case income had escaped assessment, it has equally escaped assessment if the true facts were brought to the notice of the Income-tax Officer, but he failed to appreciate them or mislaid some file and did not consider some particular facts. Again, it cannot, I think, be disputed that as this Court held in *Commissioner of Income-tax, Bombay v. P.N. Contractor*², if an assessment is based on a view of the law held to be correct by High Courts in India but subsequently within the year allowed by Section 34 held by the Privy Council to be incorrect and by reason of that revealed change in the law it appears that some income has escaped assessment, that is a good ground for serving a notice under Section 34, and re-assessing the assessee. But if one accepts that view, it is very difficult to say that the case would not have fallen within Section 34, if the decision of the higher tribunal had been given before the assessment though the Income-tax Officer did not know of the decision, or had failed to appreciate it. It seems to me very difficult on the language of Section 34 to say that in order to hold that income may have escaped assessment, there must have been either some fresh facts brought to the notice of the income-tax authorities or some change in the law and to hold that a mere change of opinion by the Income-tax Officer will not be sufficient to found a case under the section.

The Privy Council in a recent case, *Commissioner of Income-tax, Bengal v. Mahaliram Ramjidas*³, in which they were dealing with a decision of the Calcutta High Court in which it had been held that before a notice can be given under Section 34, the Income-tax Officer must hold some sort of judicial inquiry to satisfy himself that a proper case exists, were not prepared to accept that view and held that to enable an Income-tax Officer to initiate proceedings under Section 34 it is enough that the Income-tax Officer on the information which he has

(1) (1936) 4 I.T.R. 209.

(3) (1940) 8 I.T.R. 442.

(2) (1937) 5 I.T.R. 338.

before him and in good faith considers that he has good ground for believing that the assessee's profits have for some reason escaped assessment, or have been assessed at too low a rate. So that, a notice can be served if the Income-tax Officer is *bona fide* of opinion that the income has escaped assessment. High Courts in this country have held that an Income-tax Officer or his successor is entitled under Section 34 to re-assess the income, merely because he thinks that owing to some mistake in the first assessment income has escaped assessment. That has been held by the Madras High Court in *Commissioner of Income-tax v. Raja of Parlakimedi*¹, by the Lahore High Court in *Amir Singh Sher Singh v. Commissioner of Income-tax*², and by the Calcutta High Court in *P. C. Mallick and D C Aich In re*³, whilst there is a dictum of Sir George Rankin in *Anglo Persian Oil Co., Ltd. v. Commissioner of Income-tax*⁴ to the effect that Section 34 is applicable to put right an assessment by which a deduction has been improperly allowed. The Income-tax Tribunal has based its decision in this case very largely on that dictum. The effect of those decisions appears to be to allow Section 34 to be used as a section giving power to the Income-tax Officer to revise his own decision or the decision of his predecessor and in view of the other provisions for revision in the Income-tax Act, *e.g.*, Section 33 and Section 35, it is rather strange that Section 34 should have that effect. But, as I have already pointed out, if it be once admitted that an assessment may be reopened under Section 34 (and the language seems to make such an admission inevitable) it is very difficult to draw the line in any way, and to say that it can only be reopened on a particular ground, such as change of facts, or alteration in the law. I may say that even if I disagreed with the decisions, which I do not, I should not be prepared to differ from decisions of other High Courts on an Act of this sort which applies throughout British India.

In my opinion, therefore, the notice under Section 34 was justified, but that does not dispose of the matter. Income cannot be held to have escaped assessment merely on the *ipse dixit* of the Income-tax Officer. As held by this Court in *Commissioner of Income-tax, Bombay v. Manohar*⁵, it is for the Income-tax Officer to establish to his own satisfaction on the assessment and subsequently before any Appellate Tribunal that income has escaped assessment; it is not for the assessee to prove that the original assessment was right and that no income has escaped assessment.

The facts of this case are peculiar. The Tribunal has held that before the Income-tax Officer on the occasion of the first assessment the

(1) (1925) 2 I.T.C. 104.

(3) (1940) 8 I.T.R. 236.

(2) (1935) 3 I.T.R. 171.

(4) (1933) 1 I.T.R. 129.

(5) (1935) 3 I.T.R. 372.

assessee's books for the Maru year 1990-91 were produced though this was denied by the Commissioner. When the second assessment was made, which was not till 1940, more than six years after the close of the Maru year 1990-91, the books of that year were not available. The position is discussed in paragraph 8 of the assessee's grounds of appeal where they point out that there have been many changes in the Income-tax Officer whose duty it was from time to time to deal with their assessment, and they say that they did produce the books for the Maru year 1990-91 at the original assessment and on subsequent occasions, but when it came to the last assessment, they had sent the books to their native place, where they had been destroyed as being more than six years old. There is no reason to doubt that statement. The Tribunal has held as a fact that all these books were produced at the original assessment. So that, it really comes to this, that the second Income-tax Officer has differed from the first not merely on the same material, but on much less material, than the first officer had. He holds without the books of 1990-91 that there was no straddle business in that year and without those books it seems difficult to arrive at that conclusion, when an officer who saw the books arrived at an opposite conclusion. The Appellate Tribunal no doubt has agreed with the second officer's conclusion and they say that notwithstanding that the books for the Maru year 1990-91 were originally produced, the fact remains that "we have little or no evidence of any straddle business done by the appellants in London in the year in question". But that is really throwing upon the assessee the burden of proving that income has not escaped assessment and that burden is thrown upon them at a time when, through the delay in dealing with the re-assessment, the necessary material is not available. In my opinion, an Income-tax Officer is not entitled to give a notice saying that income has escaped assessment, thereafter to wait for three years and then when the relevant books have been destroyed say that the assessee has failed to prove that the income has not escaped assessment. Therefore whilst I agree that the notice under Section 34 was justified though no fresh material was available, I do not agree that there is evidence that any income had escaped assessment. In my opinion the Tribunal ought to have held that there was no evidence on which the second Income-tax Officer could hold that any income had escaped assessment.

I would, therefore, answer the second question in the negative.

The Commissioner to pay three fourths of the costs. Certificate to issue that no question under Section 205 of the Government of India Act arises in this case.

KANIA, J.—Two questions have been submitted by the Tribunal for the determination of the Court. The necessary facts, reasons and our conclusion have been stated in respect of the first question by the learned Chief Justice in his judgment and I have nothing more to add to that.

As regards the second question, the facts are these. The assessment year was 1936-37 and the accounting year S. 1991 (Maru) was from the 8th of November 1934 to the 27th of October 1935. The sole item under which the assessees were assessed was business. According to them they had transactions in silver in Bombay and they were also doing straddle business in silver in Bombay and London. Straddle business done in Bombay during the last three months of Maru 1991 (which, by the very use of the word 'straddle', must mean carry over so as to set off the outstanding business in London) showed that in carrying out the business the assessees had paid in the market certain amounts. The amounts so paid were debited in their ledger. After considering all the facts the Income-tax Officer made the assessment order on the 9th July. Before doing that, as the record shows, the assessees had produced their books of account of Samvat 1990-91 and also of 1991-92. Not only that but an Examiner's report on those books was submitted to the then Income-tax Officer before he made the assessment. That officer came to the conclusion that the loss shown in the ledger of S. 1990-91 appertained to the transactions of S. 1991-92 and allowed the assessees to set off the debit items mentioned above against the profits for S. 1991-92. On no other footing he could allow a set off in respect of that loss against the business of S. 1991-92. It must be presumed that the Income-tax Officer was aware of the relevant provisions of the Income-tax Act.

Thereafter, on the 22nd of March 1938 a notice under Section 34 was issued on the assessees to start re-assessment proceedings. The assessees appeared before the Income-tax Officer. In para 8 of the grounds of appeal before the Appellate Tribunal, they have stated that in the course of re-assessment, books of S. 1991-92 were called for and examined. The officer did not ask the assessees to produce the books of S. 1990-91. Before the officer could pass orders the case was transferred to another Income-tax Officer. That officer again never called for the books of S. 1990-91. He examined only the books of 1991-92. Before he also could pass an order the case was again transferred to the Income-tax Officer, Section VII, Central, and it was only in 1940 that the officer asked to see the books of S. 1990-91 (1934-35). The assessees further stated that their books according to their usual practice after the assessment was made by the Income-tax Officer were

sent away to their native place except for one preceding year. They had accordingly sent over the books for S. 1990-91 to their native place after the assessment order was made on 9th July 1937. When in 1940 the demand for the reproduction of these books was made they made inquiries and it was found that the same were destroyed along with other old books as they had been moth-eaten. These facts which are set out in the grounds of appeal are not controverted. In 1940 without seeing the books of S. 1990-91 and without any additional or new evidence the Income-tax Officer held that the straddle transactions were not proved and the debit items mentioned above appertained to the business of the previous year. He was therefore of opinion that the allowance made in making the previous assessment order was unjustified and had escaped assessment. The Tribunal accepted the facts about the production of the books previously but appears to be pressed to consider the rest of the evidence. From the judgment of the Tribunal it is clear that before them also it was not alleged that any additional or new evidence was considered in making the re-assessment. In the course of its judgment the Tribunal observed that the transactions were independent and the method of accounting adopted had been altered. Admittedly these surmises were based on the fragmentary materials put before them and without considering and in the absence of the assessee's books for S. 1990-91.

The question is whether under these circumstances the order made by the officer in 1940 on the basis that the income had escaped assessment, is justified. To put it in brief, the first officer had evidence of A, B, C and D before him and he came to the conclusion that the transactions were straddle transactions and that the loss on account of these transactions entered in the books of S. 1990-91 should be allowed to be set off against the business profits of S. 1991-92. When re-considering the matter under Section 34, the Income-tax Officer in 1940 had before him only three out of the above mentioned four pieces of evidence and no other evidence at all. On that evidence only he held that the item of Rs. 2,95,619 had escaped assessment. In my opinion, the record thus clearly shows that there was no evidence before the Income-tax Officer or the Tribunal to hold that any income had escaped assessment. The question of law about the application of Section 34 could arise only if on the same materials at least the second officer had come to a different conclusion.

On the question of interpretation of Section 34, considerable time has been spent and I think it is desirable under the circumstances to express my opinion on it. I may notice that I have not been a party to any previous decision on Section 34, although I am bound by the

opinion of the Benches of this Court expressed in considering this section. It may also be noticed that the present discussion centres round Section 34 of the Act as it existed before the amendment. I make this clear, because the words of the amended section correspond more to the section of the English Act in force.

Under Section 34 the relevant words are that if for any reason income, profits or gains chargeable to income-tax has escaped assessment, the Income-tax Officer may at any time within one year adopt proceedings by issuing a notice similar to the one under Section 22 of the Income-tax Act.

The first case on this point, to which our attention was drawn, is *Commissioner of Income-tax v. Raja of Parlakimedi*¹. It was decided by the Madras High Court. The income of certain houses had not been assessed in a particular year and in a subsequent year on a reconsideration of the matter by another officer, it was held that the income of the houses was assessable. The question arose whether it could be re-assessed retrospectively. In dealing with the question Coutts Trotter, C.J., relied on the words "too low a rate" used in Section 34 for the construction of the first part of Section 34 which deals with escaped assessment. That learned Chief Justice observed that because a lower rate of assessment could not be due to mere inadvertence if income had not been assessed through inadvertence, it could equally be covered by the words "escaped assessment." I respectfully differ from this line of reasoning because a lower rate of assessment is not necessarily due to mere inadvertence. It may be due to various other considerations and not mere inadvertence.

The next case is *Anglo-Persian Oil Co. v. Commissioner of Income-tax*², where Rankin, C.J., had occasion to consider this Section 34. Although the point did not arise directly before him, he expressed the opinion on the meaning of that section and stated that the words were wide enough to cover a deduction which had been improperly allowed. About 5 months later came the decision of the Rangoon High Court in *Commissioner of Income-tax, Burma v. U Lu Nyo*³, where three Judges of that Court came to the conclusion that the words "escaped assessment" in Section 34 did not cover the case of income which had been considered by the assessing officer and allowed to pass free or assessed in a particular way. According to them "escaped" must mean what had not been considered because once it had been considered by the income-tax authorities, it became income which was assessed. That

(1) (1925) 2 I.T.C. 104.

(2) (1933) 1 I.T.R. 129.

(3) (1933) 1 I.T.R. 373.

view was considered too narrow and not accepted by the Bombay High Court in *Commissioner of Income-tax, Bombay v. Manohar*¹.

In between there arose an occasion for the Privy Council to refer to Section 34 in *Sir Rajendranath v. Commissioner of Income-tax*². As I read that judgment, it does not cover the point before us at all. In that case an assessee had made his return and while the consideration of that return was pending another assessee's assessment was considered. It was found that a certain item which was included in that (second) return should not be included in that return but should be put in the first return. The argument before the Privy Council was that as one year had expired there was no justification for including this item under the first return. That argument was negatived, and, in my opinion, there can be no two opinions on the question. The only reference to Section 34 made by the Privy Council was because it was used as an argument in support of the contention urged before them. Their Lordships had no occasion to consider the effect and meaning of the words "escaped assessment." They only negatived the contention that the words "has escaped assessment" were equivalent to "has not been assessed".

In the case of *Commissioner of Income-tax, Bombay v. Manohar*¹ a Bench of this Court had occasion to consider the operation of Section 34. The facts found there were as follows: The first officer had according to his opinion fixed a certain percentage of the price of gold and silver as profit to be assessed. Obviously that was based on what one might call a rule of thumb. After some time a notice under Section 34 was issued and the second officer in his opinion thought that a higher rate should be taken for calculating the profit. That was equally another rule of thumb laid down by that officer. When the matter came before the Court, the Bench decided that this was not covered by Section 34. The burden of showing that income had escaped assessment (in the sense that the Income-tax Officer had some evidence before him to justify the conclusion that the income had escaped assessment) was on the Commissioner. The Bench found that there was no evidence except mere opinion, which, to put it at its highest, was a surmise. The Court therefore held that the second assessment was not justified. This opinion of our Court, I apprehend, was not properly appreciated by the learned Judges of the Rangoon High Court in *Commissioner of Income-tax v. Dey Brothers*.³ They adhered to the view they had expressed in their previous case of *Commissioner of Income-tax, Burma v. U Lu Nyo*⁴ which, so far as the

(1) (1935) 3 I.T.R. 372.

(3) (1936) 4 I.T.R. 209.

(2) (1934) 2 I.T.R. 71.

(4) (1933) 1 I.T.R. 373.

principle was concerned was accepted by this Court in *Commissioner of Income-tax, Bombay v. Manohar*¹.

Those cases came to be considered by the Lahore High Court in *Amir Singh Sher Singh v. Commissioner of Income-tax*². The learned Judges came to the conclusion that having regard to the opening words of Section 34, *vis.*, "for any reason" there was no justification for confining the meaning of the word "escape" within any limits, and all the different meanings given to the word "escape" in Murray's Oxford Dictionary could be held applicable to the word "escape" when the matter came to be considered by the Income-tax Officer under Section 34. In *Madan Mohan Lal v. Commissioner of Income-tax*³, a Full Bench of the Lahore High Court had occasion to consider again the meaning of Section 34 in view of the different opinions so far expressed by the three High Courts, and the majority of the Judges (Dalip Singh, J., dissenting) held that the meaning given to the word "escape" in *Amir Singh Sher Singh v. Commissioner of Income-tax*² was correct. Mr. Justice Dalip Singh was of the opinion that the word "escaped" should be limited to mean "eluded notice" and should not be given all the different meanings noted against that word in Murray's Dictionary. In *In re P. C. Mallick & D. C. Aich*⁴, the Calcutta High Court had occasion to consider the construction of Section 34. In that case a testator by his will directed *inter alia* certain payments of money to be made to certain beneficiaries and annuities to certain other persons out of the income of his property. In the assessment of income-tax for the year 1933 made on the executors the Income-tax Officer allowed as a deduction a certain sum which was paid to the beneficiaries under the will. In January 1935 the Income-tax authorities came to the conclusion that the amount was improperly allowed and assessed it under Section 34 on the ground that it had escaped assessment in the year in question. It was held that having regard to the plain words of Section 34, it was impossible to say that the amount did not escape assessment in the year in question. In the course of his judgment Derbyshire, C. J., referred to a decision of this Court in *Commissioner of Income-tax v. D. R. Naik*⁵. In that case because of an interpretation of certain existing law by the Privy Council it was ascertained that a mistake of law had been committed in making the previous assessment and proceedings were considered to have been properly started under Section 34 within the prescribed time. In the Calcutta case when making the first assessment the Income-tax authorities had the figure of the

(1) (1935) 3 I.T.R. 372.

(2) (1935) 3 I.T.R. 171.

(3) (1935) 3 I.T.R. 438.

(4) (1940) 8 I.T.R. 236.

(5) (1939) 7 I.T.R. 362.

amount which they allowed before them and after considering it allowed the deduction. The learned Chief Justice held that the amount was not assessed and it was assessed because the Income-tax Officer made a mistake in 1933 which he attempted to put right in January 1935. Having regard to the general words used at the commencement of the section it was held that it was impossible to say that the amount had not escaped assessment in the year in question. The Allahabad and Madras cases do not appear to be discussed in the judgment.

In this state of the law the question is whether Section 34 gives to the Income-tax Officer a large revising power as contended on behalf of the respondent or whether it is limited only to set right what had been either overlooked or misunderstood. The cases noted above clearly show that the Madras, Lahore and Calcutta High Courts are of the view that there is no justification to limit the operation of the word "escaped" as suggested by Sir Arthur Page in his judgment in the Rangoon case. The Bombay High Court has differed from the view of the Rangoon High Court and held that the meaning given to the word "escaped" appeared to be unnecessarily narrow in that case.

Our High Court has accepted the principle that unless it found it impossible conscientiously to accept the consensus of opinion of other High Courts it would follow the construction put on a section of an Act applicable to the whole of India by the other High Courts. Acting under that principle if necessary I would agree that Section 34 had that wider application. If the matter were at large, I confess that I am not prepared to give such wide meaning to the word "escaped". Section 34, in my opinion, should be construed along with the other sections of the Act. In the ordinary course an order made after investigation by a particular officer should not at his sweet will and pleasure be allowed to be varied. There must in my view exist something either suppressed by the assessee, or a fact or point of law which he inadvertently or otherwise omitted to consider before he could proceed to act under Section 34 of the Act. It is only in those cases that the Income-tax Officer or his successor occupying the same position has a right to revise the order. A mere change of opinion on the same facts and law is not covered by the section. I admit that the words "for any reason" used in Section 34 are very wide. However I think the words used in the section must be given a reasonable meaning having regard to the other powers contained in the Act. In my view if an assessing officer felt that he had committed an error *bona fide* it is open to him to refer the case under Section 33 to the Commissioner and for the Commissioner to act on such reference. I should hesitate considerably before assuming that under Section 34 the

same Income-tax Officer had power to revise his order for one year, and, if the argument is carried to its logical extent, as many times as he liked within that year. The different meanings given to the word "escaped" in a dictionary are not all applicable to the word at the same time. The context must be looked at and the meaning appropriate under the circumstances only should be given to the word.

I agree that the second question should be answered in the negative.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

DAYALDAS KHUSHIRAM

v.

COMMISSIONER OF INCOME-TAX, (CENTRAL), BOMBAY.

BEAUMONT, C. J., and KANIA, J.

September 23, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922 AFTER AMENDMENT OF 1939)
SECS. 5, 64—INCOME-TAX (REMOVAL OF DIFFICULTIES AND VALIDATING)
ORDINANCE (IX OF 1939)—JURISDICTION—PLACE OF ASSESSMENT—
APPEAL—TRANSFER OF CASE BY COMMISSIONER OF INCOME-TAX,
CENTRAL, TO INCOME-TAX OFFICER, SECTION II, CENTRAL—WHETHER
INVOLVES QUESTION AS TO PLACE OF ASSESSMENT—WHETHER CAN BE
DECIDED IN APPEAL—SCOPE OF SECTION 64—ORDINANCE No. IX OF
1939—WHETHER VALIDATES PRIOR ORDERS.

*The assessee in Dayaldas Kushiram v. Commissioner of Income-tax, Central [1940] (8 I.T.R. 139) was assessed for the assessment year 1937-38 under Sections 23 (4) and 34 of the Income-tax Act by the Income-tax Officer, Section II (Central).** The appeals to the Appellate Assistant Commissioner and the Appellate Tribunal being unsuccessful, the assessee put in an application under Section 66 (1) and the Tribunal referred the following questions for the decision of the High Court:— (1) *Whether the order dated July 12, 1939, passed by the Commissioner of Income-tax, Central, under Section 64 (3) of the Income-tax Act, 1922, deciding the place of assessment of the petitioner, can be the subject of an appeal to the Income-tax Appellate Tribunal under Section 33 of the Act?* (2) *Whether the Income-tax Appellate Tribunal has power to entertain in appeal a question as to the place of assessment of an assessee, even in the absence of an order of a Commissioner of Income-tax under Section 64 (3) of the Act?* (3) *If either of the first two questions is*

* The facts which led to this reference are rather complicated and are stated in the judgment of the Chief Justice.

answered in the negative, whether a question as to the place of assessment put in an appeal to the Tribunal is a question of law arising out of its appellate judgment, so as to be subject matter of a reference to the High Court under Section 66 (1) of the Indian Income-tax Act, 1922? (4) Whether the Governor-General's Ordinance No. IX of 1939 (later incorporated in Section 64 of the Income-tax Act by an Amendment of 1940) has the effect of regularising or validating the proceedings of re-assessment of the petitioner for the charge year 1937-38, irrespective of whether they were initiated by the Income-tax Officer, Special Provincial Circle, without jurisdiction to make the assessment?

Held, (1) *that the order of the Commissioner of Income-tax, Central, dated July 12, 1939, was an order under Section 5 (2) and was not in fact made under Section 64 (3). Moreover Ordinance No. IX of 1939 directed that the provisions of Section 64 (1) and (2) were to be deemed not to apply and never to have applied to the assessee. Consequently question 1 did not arise;*

(2) that questions 2 and 3 also did not arise;

(3) that the re-assessment of the assessee was validly started by the Income-tax Officer, Special Provincial Circle, and Sections 2 and 3 of Ordinance No. IX of 1939 removed the invalidity of the orders made prior to the passing of the Ordinance so far as they related to the assessee.

BEAUMONT, C.J.—*The Income-tax Act does not determine the place of assessment. What it does is to determine the officer who is to have power to assess and in some cases it does so by reference to locality but an appeal would be not against an order of the Commissioner as to the place of assessment but against the order of assessment of the Income-tax Officer. Under Section 30 no right of appeal against an order under Section 64 (3) is conferred since the appeal could probably be not against an order made under Section 64 (3) but against the consequences following from such order.*

Ordinance No. IX of 1939 is retrospective in character and must be construed strictly and no case should be brought within it which is not fairly within its language.

KANIA, J.—*In respect of questions of jurisdiction the point may arise under Section 64 (3) or otherwise and the jurisdiction of the Tribunal to entertain disputed questions of jurisdiction of the particular Income-tax Officer will depend on the proper construction of the relevant sections of the Income-tax Act.*

Case referred to:

Dayaldas Kushiram v. Commissioner of Income-tax, Central (1940) 8 I.T.R. 139; 42 Bom. L.R. 414.

Case referred to the High Court by the Income-tax Appellate Tribunal, (Bombay Branch) under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by Section 92 of the Indian Income-tax (Amendment) Act (VII of 1939) for the decision of the questions of law mentioned in the head-note :—

Income-tax Reference No. 4 of 1942. The facts of the case appear in the judgment of the Appellate Tribunal and in the Statement of Case.

JUDGMENT OF APPELLATE TRIBUNAL.

Under Section 33 of the Indian Income-tax Act (XI of 1922) the Income-tax Appellate Tribunal, (Bombay Branch) (consisting of N. R. GUNDIL, Judicial Member, and P. C. MALHOTRA, Accountant Member) delivered the following judgment on 28rd August 1941 :—

“These two appeals arise out of a supplementary assessment of the appellant, Mr. Dayaldas Khushiram, for the assessment year 1937-38, made by the Income-tax Officer, Section II (Central), under Section 23 (4) and Section 34 of the Income-tax Act. The appellant applied, under Section 27, to cancel the ‘best judgment assessment’, but the Income-tax Officer dismissed the application. The appellant took that order, as well as the order of assessment, in appeal to the Appellate Assistant Commissioner who, in each case, declined to interfere. These two appeals are respectively taken from his orders, and involve common facts. They were heard together, and may be conveniently disposed of in one judgment. The facts will make a long narration. We shall therefore confine ourselves at the outset only to such as will help to outline the case, and notice others in their proper place in the course of this judgment.

2. The first assessment of the appellant for the year 1937-38 was made by the Income-tax Officer, C Ward, Section II, Bombay. The appellant did not return any income, and submitted the form of the return with the remark “Accounts not kept; income to be estimated.” Considering the past assessment which, under similar circumstances, had been made on a progressively higher income as estimated, and also the fact that the appellant had been re-assessed under Section 34 in the preceding two years, the Income-tax Officer assessed him on an estimated income of Rs. 25,000, under Section 23 (4) of the Act, on 8th October 1937.

3. In November 1938, the Commissioner of Income-tax, Bombay, Sind and Baluchistan, in exercise of the powers under Section 5 (4) of the Income-tax Act (as it then stood), appointed a set of Officers called Income-tax Officers, Special Provincial Circle. These Officers were not appointed to function over any specified local areas, but to deal with

cases of assessment that might be specifically made over to them by the Commissioner from all over the Province or area over which his own jurisdiction extended. One of them was Mr. V. T. Shah to whom the Commissioner made over the appellant's case, along with several others. The case made over was apparently the assessment for the year 1938-39 which was then due to be made. On going through the record, and, after making certain enquiries, the Income-tax Officer thought that the appellant had been under-assessed for the assessment year 1937-38. Accordingly, he commenced the present re-assessment proceeding after serving the appellant with a notice under Section 34 of the Act, on 21st December 1938. In the notice, it was expressly stated that the appellant's business income for the Samvat year 1992 had partially escaped assessment, and that from property, interest, interest on securities and dividends had wholly done so; and called upon him to make a fresh return of income from these sources. On 20th January 1939, the appellant filed a return declaring an income of Rs. 25,000, without details, with the remark "As settled and already assessed and agreed to by the Income-tax Officer, inclusive of property, dividends, interest and wife's income", implying that a proper assessment had been made by the Income-tax Officer, C Ward, Section II, and that it could not be reopened. It may also be mentioned here that by an application, dated 20th February 1939, the appellant questioned the jurisdiction of the Income-tax Officer to assess or re-assess him. On a reference under Section 64 (3) the Commissioner passed an order, dated 9th March, which will be discussed later.

4. With the advent of the amended Income-tax Act, on 1st April 1939, the organization of the Special Provincial Circle became unnecessary, inasmuch as the new sub-section (2) of Section 5 gave power to the Central Government to appoint a Commissioner of Income-tax without reference to area, and to exercise the functions of a Commissioner of Income-tax to the exclusion of a Commissioner of Income-tax appointed for specific area, in respect of cases or classes of cases that might be made over to him by the Central Board of Revenue. In exercise of these powers the Government appointed Mr. Bird as Commissioner of Income-tax (Central) without reference to area, with effect from 1st April 1939. He organised six sections, called Sections I to VI (Central), with headquarters at Bombay and appointed a set of Income-tax Officers to deal with cases that would be made over to him by the Central Board of Revenue, and, in turn, assigned by him to these Officers. One of them was Mr. Shah who was assigned Section II (Central), and was charged with the cases of the appellant's assessment and re-assessment, under Section 5 (5). In this manner, Mr. Shah who had been in charge of

the appellant's assessment as Income-tax Officer, Special Provincial Circle, continued to function over them as Income-tax Officer, Section II (Central). In June 1939, the appellant once again raised the question of Mr. Shah's jurisdiction which he referred to the Commissioner of Income-tax, Central, under Section 64 (3) of the Act. On 12th July 1939, the Commissioner made an order that Mr. Shah was "correctly vested" with the power to assess and re-assess the appellant. The appellant thereafter took the matter to the High Court of Bombay by means of a petition, under Section 45 of the Specific Relief Act, praying that the Commissioner of Income-tax, Central, and the Income-tax Officer, Section II (Central), be restrained from proceeding with his assessments. On 15th December 1939, their Lordships made the rule absolute holding that the Commissioner of Income-tax, Central, had no power under Section 5 (5) of the new Act to make over the appellant's case to the Income-tax Officer, Section II (Central), because the latter was not the Income-tax Officer for the local area in which the appellant did business and who alone could validly assess the appellant under Section 64 (1) of the Act which had not been amended to correspond with the changes in Section 5; and that consequently, the Income-tax Officer, Section II (Central) had equally no jurisdiction to make the appellant's assessments*. On 30th December following, the Governor-General promulgated Ordinance No. IX of 1939, which, broadly speaking, validated the proceedings of the Commissioner of Income-tax, Central, as well as those of the Income-tax Officers charged by him with the assessments such as those of the appellant. Shortly afterwards, a question as to the effect of the Ordinance upon the judgment already obtained came under the consideration of the Bombay High Court at the instance of another assessee similarly placed as the appellant, and their Lordships held that the Ordinance in question overrode the judgment of 15th December. Accordingly, the Income-tax Officer, Section II (Central) proceeded with the assessments, and finally re-assessed the appellant according to his best judgment on an income of Rs. 1,66,600, under Section 23 (4) of the Act owing to the appellant's failure to produce books of account, documents and papers specifically called for by repeated notices under Section 22 (4).

5. We shall first deal with the appeal from the order under Section 27 of the Act. After the appellant had filed a supplementary Return, the Income-tax Officer issued the first set of notices under Section 23 (2) and Section 22 (4), calling upon him to produce evidence in support of his return, also books of account for the Samvat year 1992, as well as all his bank pass-books, counterfoils of cheques, rent and tax bills,

* See *Dayaldas Kushiram v. Commissioner of Income-tax, Central* (1940) 8 I.T.R. 139.

Ankdas of ready and forward business and all accounts showing investments. These requisitions were repeated not less than five times, till February 1940. The only compliance that the appellant made was to produce two pass-books of the Central Bank, Zaveri Bazar Branch, and the Bank of India, respectively. The latter did not relate to the accounting period which was Samvat year 1992, and was therefore useless.

6. Under Section 27 of the Income-tax Act, the two grounds which entitle an assessee to ask for cancellation of a best judgment assessment made under Section 23 (4) are that he had no reasonable opportunity to comply, or, that he was prevented by a sufficient cause from complying, with a notice under Section 22 (4). It is only the second ground that the learned counsel has relied on. Thus the only question for decision is whether the appellant was prevented by a sufficient cause from complying with the terms of the notices. His main contention is that he does not maintain books or any kind of accounts; and that such documents that he had were duly produced by him. These documents were the two pass-books just alluded to. It is admitted that he had account with the Baroda and Allahabad Banks. But the pass-books of these accounts were not produced, and the excuse that is offered is a lapse of memory due to the accounts having been closed for some time past. Admittedly, these accounts had not been closed in the accounting year, Samvat 1992. Thus, except producing the two pass-books one of which was not relevant, the appellant failed to comply with the requisitions of the notices in question. It is argued that a compliance was out of the question, because he did not possess accounts or documents of any sort. That amounts to saying that the appellant had a sufficient cause or justification for not complying with the notices. But Section 27 of the Income-tax Act requires an assessee to prove that he was prevented by a sufficient cause from complying with the terms of a notice under Section 22 (4). The phrase "prevented by sufficient cause from complying" does not have the same meaning as "having sufficient cause for not complying." They are not convertible expressions. In other words, Section 27 can be invoked only when an assessee possesses the books and papers called for by a notice under Section 22 (4), but is prevented by a sufficient cause from producing them from the Income-tax Officer. It follows that a justification for non-compliance with the requisitions of such a notice can be no ground for cancelling an assessment under Section 27. In such a case an appellant's remedy will be a regular assessment appeal asking to be assessed under Section 23 (3) instead of Section 23 (4). This view is supported by the case of *Commissioner of Income-tax, C. P. & U. P. v. Laxminarain Badridas*¹. Therefore, it seems to us that the present application

under Section 27 was incompetent. It is also argued that the notices under Section 22 (4) were illegal having been made without jurisdiction, and that, therefore, there was no obligation on the appellant's part to comply with them. We shall presently discuss the question of illegality of the notices. Here it suffices to say that the plea of illegality as a sufficient cause for non-compliance amounts to a justification, and must also be rejected for reasons just stated.

7. Apart from this, we can scarcely believe that the appellant has not maintained books of account, or did not possess most of the rest of the documents called for. Admittedly he was doing extensive business, both ready and forward, in silver, cotton, shares, etc., in London, Shanghai, Liverpool and Bombay, through a number of brokers. In this connection, we shall refer to a couple of instances. In an account styled S. D. Chandani with the brokers M/s Jeewatlal Pratapsey, which is proved to be a personal account of the assessee, one finds total credits of over two lacs of rupees against total debits of Rs. 1,96,000. Similar is the case in the appellant's account with M/s C. B. Mehta. It is admitted that the appellant has been doing transactions not only in cash, but by means of hundies, cheques and havalas. All this colossal business cannot possibly be done without the assistance of accounts. The appellant was first brought on the list of assessees in 1930-31. He then returned a loss which he supported by a set of account books, and was not assessed to tax. He was similarly exempted in the following year. From 1932-33 onwards the books disappeared, and the appellant used to be assessed on the basis of an estimated progressively higher income, and was, in more than one year, re-assessed under Section 84. All the while he persisted in denying that he had accounts although in 1935-36 he was definitely warned to maintain them. He had to admit at a later stage of these proceedings that he had maintained note-books of his transactions, but stated that he had destroyed them as being no longer useful. A similar plea is trotted out in regard to the Ankdas of forward business, and clearing house statements of the Bullion Exchange. Speaking of the former, it is remarkable that the appellant produced some of them in the assessment years 1935-36, 1936-37, 1938-39 and 1939-40, but he pretends that he destroyed only those for the assessment year 1937-38 in question. He produced several Ankdas before the Appellate Assistant Commissioner, but cannot explain why he did not do so earlier before the Income-tax Officer. Regarding his banking accounts, we have stated before that the only relevant pass-book that he produced was that of the Central Bank, Zaveri Bazar Branch, although he had accounts with three others. He also resented the Income-tax Officer's efforts to obtain an extract of

his accounts from the Bank of India for the material period. It is, we think, unnecessary to dwell on the appellant's story longer than to say that it is highly improbable and unconvincing. The irresistible conclusion is that he deliberately failed to comply with the requirements of the notices under Section 22 (4) issued from time to time. We therefore decline to interfere with the Appellate Assistant Commissioner's order under appeal.

8. This brings us to the other, *i.e.*, the assessment appeal. At the outset, it will be well to dispose of two small points that the learned counsel for the appellant raised at the outset. In the first place, he contended that the notice under Section 34, dated 20th December 1938, was illegal on the ground that it aimed at re-assessing the income that had been already assessed in 1937 by the Income-tax Officer, C Ward, Section II. But it is clear from the assessment note of the Income-tax Officer, as well as the rest of the assessment record, that the income that was then assessed was the business income alone, exclusive of any of the other sources specified in the notice under Section 34. In view of this fact the learned counsel gave up further contest upon the point. The second contention was that the Commissioner of Income-tax, Bombay, Sind and Baluchistan, had no power to make over the case of the appellant's re-assessment to the Income-tax Officer, Special Provincial Circle, as no such case was pending in November 1938, the appellant's assessment having been completed before, as just stated. Section 5 (4) of the Act then in force gave power to the Commissioner to allocate and distribute work among his Income-tax Officers. What he did in the present case was to allocate the work of assessing the appellant to the Income-tax Officer, Special Provincial Circle. Whether he could legally do so by reason of the latter not being the Income-tax Officer of the area in which the appellant's place of business was situate is not material to the present point. Really speaking, the work thus allocated was the assessment for the year 1938-39. But the Income-tax Officer on going through the records and making enquiries thought that the appellant had been under-assessed for the year 1937-38, and, accordingly, started to make a supplementary assessment, side by side with the assessment for the year 1938-39. As far as we can see, there is nothing in Section 34 or any other provision of the Income-tax Act to prevent an Income-tax Officer in such circumstances to take action for re-assessing the assessee, provided he does so under conditions mentioned in that section, and within the time prescribed by it. To adopt any other view would be to render the machinery provided by Section 34 to set right an under-assessment wholly nugatory. Therefore the point has no substance.

9. Broadly stated, the two main questions argued in this appeal are, first, that the supplementary assessment is illegal and void *ab initio*, having been made by the Income-tax Officer, Section II (Central), without jurisdiction to assess the appellant under Section 64 (1) of the Income-tax Act; and secondly, that the assessment itself is excessive and arbitrary. Before coming to discuss the first question which is a question of law, it is necessary to consider a preliminary objection taken by the learned departmental representative to the appellant's raising the question of jurisdiction in appeal before this Tribunal. Mr. Mehrotra contends that under Section 64 (3) of the Act the Commissioner of Income-tax alone has the power to determine a question as to the place of assessment of an assessee, except in certain circumstances in which it may be exercised by Commissioners of more provinces than one, or the Central Board of Revenue; and that it is not open to an assessee to raise the point of jurisdiction, or call in question the Commissioner's order in this respect, either in an appeal to the Appellate Assistant Commissioner or the Appellate Tribunal. We think that the position taken up by the learned departmental representative is correct.

10. Taking up the second of the two points in this case we have two orders passed by two different Commissioners of Income-tax under Section 64 (3) of the Act; the first, dated 9th March 1939, by the Commissioner, Bombay, Sind and Baluchistan, and the second, dated 12th July 1939, by the Commissioner of Income-tax, Central, on respective references made by Mr. Shah as Income-tax Officer, Special Provincial Circle, and Income-tax Officer, Section II (Central). The first order is:—

“A question of proper place of assessment having arisen, under Section 64 (3) of the Income-tax Act the assessment of the assessee for the year 1938-39 is made over to the Income-tax Officer, C Ward, Section II Bombay.”

Unfortunately, the order is altogether silent with regard to the re-assessment of 1937-38, and it is difficult to conjecture the reason for the omission. If the Commissioner thought that the Income-tax Officer, Special Provincial Circle, had no jurisdiction to make the appellant's assessment for 1938-39, it is not easy to imagine how he could hold otherwise in the case of the supplementary assessment of the same assessee that was being made side by side with the other by the same Income-tax Officer, under the same circumstances. We are not at the present moment concerned with the effect of the omission upon the present proceeding. But it must be held as a fact that there was no order determining the place of appellant's re-assessment under Section

64 (3) of the Income-tax Act. The second order, however, specifically deals with the point. Mr. Bird held that the Income-tax Officer, Section II (Central), was "correctly vested" with the power to levy the appellant's re-assessment for the year 1937-38, and the assessments for 1938-39 and 1939-40 which last had then become due. The appellant successfully contended before the High Court of Bombay that the Commissioner of Income-tax, Central, had no power to direct his assessment to be made by the Income-tax Officer, Section II (Central), Bombay, and that the latter had equally no jurisdiction to assess him, having regard to Section 64 (1) of the Act. But it is conceded that the Governor-General's Ordinance IX of 1939 validated the acts of both these Officers in connection with the assessments at any rate, from 1st April 1939. Mr. Bird's order in question, having been passed on 12th July following, must be taken to be equally validated, and must, for the present purpose, be regarded as a valid order. Thus, we have an order of the Commissioner of Income-tax, Central, under Section 64 (3) of the Act holding that the Income-tax Officer, Section II (Central), had jurisdiction to assess and re-assess the appellant.

11. The material provisions of the Income-tax Act that deal with the place of assessment of an assessee are Section 64, sub-sections (1) and (2), in which no change was made by the amendments of 1939. It may be mentioned that amendments were made in these sub-sections in 1940 to cover a case like the present, but we are not concerned with them in this case. Under sub-sections (1) and (2) as they stood at the material time, an assessee had a right to be assessed by the Income-tax Officer of that area, which means the local area, in which he did business or resided. Sub-section (3) is to the effect that where any question arises as to the place of assessment such question shall be determined by the Commissioner, and, in certain circumstances, by more Commissioners than one, or, the Central Board of Revenue. It is therefore clear that in case of a dispute regarding the place of assessment, that is to say, the jurisdiction of the Income-tax Officer to assess a particular assessee, the Commissioner of Income-tax is the sole authority to decide it. Now Section 30 of the Income-tax Act gives an assessee a right of appeal to the Appellate Assistant Commissioner against the Income-tax Officer's orders, but such a right is confined to certain points only, *i.e.*, those enumerated in the section. The right has been enlarged by the section as amended in 1939, but those points do not cover a decision of the Commissioner under Section 64 (3) in virtue of which an Income-tax Officer assumes jurisdiction to assess an assessee. Evidently, the intention of the Legislature in not allowing an appeal from a Commissioner's order under Section 64 (3) was to obviate the

anomaly of an Assistant Commissioner sitting in appeal over the orders of the superior officer. Doubtless, under Section 30 an assessee may appeal to the Assistant Commissioner denying his liability to be assessed under the Act, but it has been substantially held by the decided authorities to which we shall presently refer that the phrase does not cover a point of jurisdiction such as the one taken in this case. The powers of the Appellate Tribunal are defined by Section 33 of the amended Act. An appeal lies to the Tribunal from an order passed by an Appellate Assistant Commissioner under Section 28 or 31. The latter section is alone material for the present purpose. An order under Section 31 can be passed by the Assistant Commissioner only in appeal provided by Section 30. Therefore, if an order of the Commissioner under Section 64 (3) determining a point of jurisdiction cannot be the subject of an appeal under Section 30, it cannot equally be the subject of an Appellate Assistant Commissioner's order under Section 31; and consequently, the Tribunal has no power to entertain an appeal on that point under Section 33. That is the view taken by the Allahabad High Court in two cases—*Seth Kanhaiyalal v. Commissioner of Income-tax, C. P. and U. P.*¹ and *Seth Kanhaiyalal Goenka, In re*². In both these cases their Lordships held that an assessee had no right of appeal from an order passed by the Commissioner of Income-tax under Section 64 (3) of the Income-tax Act; and also that there was no power in the High Court to interfere with such an order, on a reference under Section 66. In the present case the appellant raised the point in his appeal before the Appellate Assistant Commissioner who also dealt with it, probably without adverting to the limited right of appeal under Section 30. But that will make no difference to the appellant's case. The learned counsel, however, pointed out that the question of jurisdiction was raised and decided by the High Court of Bombay in the appellant's petition in *Dayaldas Khushiram v. Commissioner of Income-tax, Central*³ notwithstanding the contrary view expressed by the Allahabad High Court. On the other hand, the learned departmental representative tried to distinguish the case from the latter pointing out that the appellant's petition was under Section 45 of the Specific Relief Act, and not a reference under Section 66 of the Income-tax Act. But we think that a better answer to the learned counsel's argument will be that we are at the moment not considering the powers of the High Court, but those of the Appellate Tribunal which is constituted under the Income-tax Act, and whose powers are defined and circumscribed by Section 33 (1). Those powers do not permit our entertaining a question of jurisdiction such

(1) (1937) 5 I.T.R. 739.

(2) (1941) 9 I.T.R. 25.

(3) (1940) 8 I.T.R. 139.

as the one that has been raised by the appellant. We therefore hold that the point cannot be taken in appeal before us.

12. In the view that we take of this question it should be unnecessary to deal with the learned departmental representatives's first point that, even in the absence of a Commissioner's order under Section 64 (3), neither the Appellate Assistant Commissioner nor the Appellate Tribunal has power to entertain an appeal from an Income-tax Officer's wrong assumption of jurisdiction. But since we are invited to express an opinion on that point, we think that the contention is correct. Under Section 64 (3) of the Act, it is the Commissioner or the Central Board of Revenue alone that has the power to determine the place of assessment, and no other authority is vested with that power. Therefore, it seems to us that in a case of wrong assumption of jurisdiction by an Income-tax Officer, the only remedy of the assessee is to get the question determined by the Commissioner.

13. This conclusion should have sufficed to dispose of the first of the two main points, but we would prefer to deal with it on the merits also. The learned counsel's main argument is focussed on the scope of the Validating Ordinance IX of 1939. It contains three sections which we shall briefly notice. It is expressed to be an Ordinance for the removal of certain difficulties experienced, and for validating certain proceedings taken, in connection with assessments of income for the purposes of the Indian Income-tax Act, 1922. Then the preamble recites that an emergency has arisen which makes it necessary to provide for the removal of those difficulties. The difficulties were obviously those that were created by the judgment of the High Court of Bombay in the appellant's petition under Section 45 of the Specific Relief Act. Section 2, clauses (a) and (b), of the Ordinance provide that sub-sections (1) and (2) of Section 64 of the Indian Income-tax Act, 1922, shall not apply and shall be deemed never at any time to have applied to any assessee on whom an assessment or re-assessment for the purposes of that Act has been or is being made in the course of any case or class of cases in respect of which a Commissioner of Income-tax appointed without reference to area under sub-section (2) of Section 5 of the said Act is exercising functions of a Commissioner of Income-tax under the said Act, or where by any distribution or allocation of work made by the Commissioner of Income-tax under sub-section (5) of Section 5 of the said Act a particular Income-tax Officer has been charged with the function of assessing that assessee. There is no doubt or dispute that the description of an assessee contained in these clauses includes the present appellant. Then the section goes on to lay down a very important provision:—"But the

assessment of such person, whether the proceedings for such assessment began before or after the first day of April 1939, shall be made by the Income-tax Officer for the time being charged with the function of making such assessment by the Commissioner of Income-tax to whom he is subordinate." Obviously, the Income-tax Officer referred to in these words was the Income-tax Officer, Section II (Central). The judgment of the Bombay High Court directed that Officer not to proceed with the assessment of the appellant, and the Ordinance directed him to proceed with it. Thus the Ordinance validated the proceedings taken and the assessment made by the Income-tax Officer, Section II (Central).

14. The learned counsel, however, pointed out that the proceedings of the appellant's re-assessment were initiated under the Income-tax Act before its amendment. He divided the entire proceedings into two parts, *i.e.*, those initiated and carried on under the old Act up to 31st March 1939; and those that were continued under the amended Act from 1st April 1939 onwards, and contended that the Ordinance in question only validated the latter. He tried to support this position relying upon clauses (a) and (b) of Section 2 of the Ordinance which speak of the functions of a Commissioner of Income-tax appointed without reference to area under Section 5 (2) of the amended Act, and the Income-tax Officer charged by him with a particular assessment under Section 5 (5). He stressed that these sections and sub-sections are the sections and sub-sections of the amended Income-tax Act, which came into force on 1st April 1939. Therefore, while conceding that the Ordinance had the effect of validating the proceedings of the appellant's re-assessment on and from 1st April 1939, it was contended that it had no retrospective effect upon those prior to that date; so that, if the latter were invalid from the start they could not be regularised or validated by the Ordinance in question. The first question therefore is whether, as a matter of fact, the proceedings of the appellant's re-assessment commenced in November 1938 were invalid, being contrary to law. For this purpose it is necessary to consider the provisions of Section 5 (4) and Section 64 (1) of the Income-tax Act as they stood at the material time. Under Section 5 (4), a Commissioner of Income-tax had power to allocate or distribute the work of assessment among his different Income-tax Officers. But Section 64 (1) gave a right to an assessee to be assessed by the Income-tax Officer of the area, *i.e.*, the local area, in which his place of business was situate. This right of an assessee was safeguarded by restricting a Commissioner's power of making over an assessment from one Income-tax Officer to another by providing that

he could distribute or allocate the work in this manner provided that there were two Income-tax Officers appointed for the same area. In the present case, the Commissioner could make over the appellant's case to the Income-tax Officer, Mr. Shah, if he had been an Income-tax Officer of the area, *i.e.*, C Ward, Section II, Bombay, in which, admittedly, the appellant's place of business was situate, and if there was another Income-tax Officer functioning over the same area. But it is admitted that Mr. Shah was not appointed for any specific area, but to a much larger area called the Special Provincial Circle which was co-extensive with that over which the Commissioner, Bombay, Sind and Baluchistan, exercised jurisdiction. There is thus no escape from the conclusion that the Income-tax Officer, Special Provincial Circle, had no jurisdiction over the appellant's assessment or re-assessment. That is also implied in the Commissioner's order, dated 9th March 1939, by which he made over the appellant's assessment for 1938-39 back to the normal Income-tax Officer.

15. But this conclusion does not avail the appellant in this case. The learned counsel's argument might have held the field if Section 2 of the Ordinance did not contain the concluding portion which we have quoted before. Those words definitely directed the Income-tax Officer charged by the Commissioner of Income-tax, Central, with assessment such as that of the appellant to proceed with and make the assessment or re-assessment, whether the proceedings began before or after the 1st day of April 1939. Thus, in our opinion, those words validated the assessments made by the Income-tax Officer, Section II (Central), irrespective of the validity or otherwise of the proceedings taken before 1st April 1939. Further, Section 3 of the Ordinance also furnishes a complete answer to the appellant's contention. It is to the effect that no assessment made in accordance with Section 2 before the commencement of the Ordinance and no proceedings taken in *course of or for the purposes of so making an assessment* before the commencement of the Ordinance shall be or continue to be invalid by reason of anything contained in Section 64 of the Indian Income-tax Act, 1922. The words "before the commencement of the Ordinance" do not limit its operation to the proceedings taken from 1st April 1939 alone. They clearly cover also those that were taken at any time before, provided they were continued and the assessment was made in accordance with Section 2.

16. Lastly, it is contended that, at any rate, there was no proceeding for re-assessment of the appellant under Section 34 before the Income-tax Officer, Section II (Central), such as could be validated by the Governor-General's Ordinance. We are afraid that this contention is mainly based upon an erroneous notion as to the effect of the order passed by the Commissioner of Income-tax, Bombay, Sind and

· Baluchistan, on 9th March 1939, under Section 64 (3) of the Income-tax Act, in regard to the assessment proceedings of the appellant. The learned counsel appears to think that the order in question related to the transfer of the present re-assessment proceedings of 1937-38 to the Income-tax Officer, C Ward, Section II, Bombay, along with the assessment of 1938-39. On this supposition he argued that no sooner the re-assessment proceedings went back to the normal Income-tax Officer than the action taken by the Income-tax Officer, Special Provincial Circle, without jurisdiction came to an end; so that a further action for re-assessment could only be taken by issuing a fresh notice under Section 34: that no such notice having issued within the period of one year prescribed by Section 34 as it then stood, *i.e.*, one year from the end of the assessment year 1937-38, the proceedings could not be revived; and that therefore there was no proceeding under Section 34 for re-assessment of the appellant when his case was made over to the Income-tax Officer, Section II (Central), on 1st April 1939. But we have made it plain before that the Commissioner's order, dated 9th March 1939, related to the transfer of the appellant's assessment for 1938-39 alone, and left the question undecided as to the present re-assessment proceedings. Therefore, rightly or wrongly, the re-assessment proceedings for 1937-38 were left with Mr. Shah, Income-tax Officer, Special Provincial Circle, without any order in regard to their transfer. The same Officer came to be appointed as Income-tax Officer, Section II (Central), on and from 1st April 1939, so that there was a continuity of the proceeding taken in November 1938, without there being any termination or break such as the one that the learned counsel assumed. Thus the Income-tax Officer, Special Provincial Circle, initially charged with the re-assessment for 1937-38, continued to hold charge of it from 1st April 1939, although under a different designation, in virtue of the Commissioner's order. Therefore, no question of initiation of a fresh proceeding under Section 34 arises in this case. Further, Section 3 of the Ordinance is clearly to the effect that no proceeding taken in course of or for the purpose of so making an assessment before the commencement of the Ordinance shall be or continue to be invalid by reason of anything contained in Section 64 of the Indian Income-tax Act, 1922. We therefore think that, as long as the appellant's re-assessment proceedings were started before the commencement of the Ordinance and were completed in accordance with Section 2 of it, no question of invalidity can arise by reason of any break in these proceedings, even if there was any. Here it may be noted that the normal Income-tax Officer, C Ward, Section II, Bombay, as a matter of fact, placed in charge of the appellant's re-assessment of

1937-38, but it is equally clear from the record that that was not by reason of any transfer of that proceedings from the Income-tax Officer, Special Provincial Circle. It appears that the latter was temporarily absent from his duties, and that consequently the Commissioner made an order, dated 1st April 1939, placing Mr. Variava, Income-tax Officer, C Ward, Section II, in charge of the duties of the Income-tax Officer, Special Provincial Circle, in addition to his own. Thus the point made by the learned counsel fails.

17. The only remaining question argued in this appeal is regarding the quantum of assessment. It is contended that the Income-tax Officer did not proceed in a judicial manner in estimating the appellant's assessable income, and that the estimate is unfair and arbitrary. We have detailed before the circumstances in which the assessment came to be made under Section 23 (4) of the Income-tax Act, and it is unnecessary to repeat them. Briefly speaking, the appellant's persistent non-compliance with the requisitions under Section 22 (4) from time to time left the Income-tax Officer no alternative except to assess the appellant according to his best judgment. Speaking of judicial fairness, it must be admitted that an Income-tax Officer must proceed in a judicial spirit and come to a fair and reasonable conclusion upon ascertained facts, although he is not a Court, and, is to a certain extent, a Judge in his own case. At the same time, it is absurd for a person, who, as in this case, has presumably books of account and other proof and deliberately withholds them to complain of not being judicially treated. Further, as observed by their Lordships of the Privy Council in *Commissioner of Income-tax, C. P. & U. P. v. Laxminarain Badridas*¹, a best judgment assessment must necessarily be a matter of some guess-work and to a certain extent arbitrary also. But Section 23 (4) places an Income-tax Officer in a position to make such guess-work; and if it is established that an assessment is made after a proper enquiry and an honest exercise of judgment it will not be open to interference by a higher authority. In the present case, we are fully satisfied that far from being random the assessment was made after an exhaustive enquiry as far as it was practicable, as the Income-tax Officer's detailed notes clearly show. He called for and examined the books of various parties with whom the appellant had dealings in his own name and also in the names of his various nominees, and based his estimate upon the results so obtained. In short his proceedings are, to our mind, characterized by fairness and impartiality which the appellant's case very little deserved. Indeed, a part of the assessment is based on ascertained facts, and in that respect it looks to be more an assessment under Section 23 (3) than under Section 23 (4).

(1) (1937) 5 I.T.R. 170.

And if we have slightly interfered with it, the interference is not owing to any error of principle but an error of detail on the part of the Income-tax Officer.

18. We shall briefly review the material facts upon which the Income-tax Officer made the assessment. For that purpose we propose to reproduce a statement of "approximate" profit and loss which the assessee produced before the Income-tax Officer, on 11th August 1939, that is to say, 8 months after he had submitted his supplementary return. It is :—

| Approximate profit. | | Approximate loss. | |
|------------------------|-----------------|-------------------------------|-----------------|
| | Rs. | | Rs. |
| M/s Jiwatlal Pratapsey | ... 47,500 | Sitaram Biyani | ... 1,700 |
| Wadilal Chunilal | ... 33,000 | Sakalchand Damodar | ... 1,300 |
| Vithaldas Thakoredas | ... 13,000 | C. B. Mehta & Co. | ... 63,000 |
| Ambalal Chanda | ... 5,600 | Loss in Indore Cotton through | |
| Bisheshwarlal Chiraw | ... 12,500 | Miscellaneous parties | ... 5,000 |
| Magniram Hemraj | ... 4,000 | Vishandas Khushiram | ... 23,000 |
| | | | ... 94,000 |
| | | Estimated expenses | ... 2,400 |
| | | | ... 96,400 |
| | | Balance of profit | ... 19,200 |
| | <u>1,15,600</u> | | <u>1,15,600</u> |

It will be seen that the net profit of Rs. 19,200 shown by the statement fell substantially short of Rs. 25,000 which the appellant showed in the supplementary return.

19. The Income-tax Officer started by verifying these figures from the books of various parties mentioned in the statement, i.e., such books as they could produce, or chose to produce, before him. As regards the alleged losses incurred in respect of transactions in Indore cotton and paid to the appellant's brother Vishandas Khushiram, no books were forthcoming. The results of the Income-tax Officer's verification may be summarized in a tabular form as below :—

| Profits. | | Losses. | |
|------------------------|-----------------|---------------------|---------------|
| | Rs. | | Rs. |
| M/s Jiwatlal Pratapsey | ... 47,003 | Sitaram Biyani | ... 1,228 |
| Wadilal Chunilal | ... 33,000 | Sakalchand Damodar | ... 1,312 |
| Vithaldas Thakoredas | ... 13,225 | C. B. Mehta & Co. | ... 61,765 |
| Ambalal Chanda | ... 5,665 | Indore Cotton | ... Nil |
| Bisheshwarlal Chirawa | ... 13,588 | Vishandas Khushiram | ... Nil |
| Magniram Hemraj | ... 4,580 | | |
| | <u>1,17,061</u> | | <u>64,245</u> |

The slight excess in the figure of the total profits over that shown by the appellant's own approximate statement is not in contest, nor are the figures representing the losses in the first three cases. The dispute

remains in regard to the last two items alone. The Income-tax Officer disallowed them in the absence of proof. We shall consider this part of the case presently.

20. The Income-tax Officer did not accept the result on the profit side remarking that the appellant had earned a large income in undisclosed cotton and share businesses through various brokers, chief among them being M/s Jiwatlal Pratapsey. It is contended on behalf of the respondent that Rs. 47,003 represent the appellant's profit from silver transactions alone. On the other hand, the appellant maintains that this figure represents the net profit from all his transactions with M/s Jiwatlal Pratapsey. Thus the main contest in this case is focussed upon the appellant's transactions with M/s Jiwatlal Pratapsey.

21. Admittedly, the appellant speculated in cotton through the brokers in question. The account maintained in the appellant's own name in their books in this respect shows a loss of Rs. 4,650. But the respondent contends that the appellant made large profits in the accounts of his two nominees Shrichand Nandlal and V. Beharilal. Similarly, it is said that he made equally large profits in share business in the account maintained in the name of S. D. Chandani, V. Beharilal, Hariram Shrichand, V. K. Chabaria and Hariram Vishandas. The appellant, however, denied his having any connection with these several accounts.

22. Therefore, it is necessary in the first place to see whether all these accounts are really those of the appellant. He has two brothers, Hariram and Vishandas. Shrichand, Nandlal and Beharilal are the three minor sons of Hariram. Thus Shrichand Nandlal is apparently an account in the joint names of the two of the appellant's nephews. The appellant's wife's name is Mrs. Saduribai, and her surname is Chandani *alias* Chabaria. Thus S. D. Chandani would stand for Saduribai Dayaldas Chandani. The fact that these several persons are appellant's close relations is not disputed. But the appellant's contention is that his brother Hariram himself might have dealt with the brokers in the names of his two sons, sometimes combining them with his own. As regards S. D. Chandani, it is suggested that it is the name of the appellant's niece, *i.e.*, daughter of Vishandas. But it is very curious that she should be a namesake of the appellant's wife. We should have been most reluctant to countenance an inference in favour of the identity of the several accounts with that of the appellant, if the respondent's case had solely rested upon the close relationship. But there is both direct and circumstantial proof going to support the view that these several accounts were the appellant's own, and that he was himself operating them. In the first place, we have a note of the

Income-tax Officer at the foot of the assessment order to the effect that both Seth Jiwatlal Pratapsey and his munim admitted before him that business in all these accounts was done by the appellant himself. Further intrinsic proof is provided by the brokers' books in connection with these transactions. We shall cite only a few instances more important than the rest. The Shrichand Nandlal account was opened on 9th June 1936 by no less a person than the appellant, and on that day a transfer of a contract of purchase of 1,500 bales of cotton was made from his own account to the other, at his instance. Next, we have a transfer entry of Rs. 18,000 from Shrichand Nandlal account to the credit of S. D. Chandani account on Bhadarwa, Sud 8. Thirdly, a sum of Rs. 3,000 received by M/s Jiwatlal Pratapsey on behalf of the appellant from M/s Vithaldas Thakoredas is found credited into S. D. Chandani account. Fourthly, a number of shares which the appellant bought through M/s Jiwatlal Pratapsey are entered in the name of S. D. Chandani in their books, and the purchase price is found paid out of this account. Fifthly, on 28th July 1936, a sum of Rs. 2,000 is credited in the appellant's silver account by making a corresponding debit in the S. D. Chandani account. Lastly, the price of several Tata deferred shares bought by the appellant is paid out of the S. D. Chandani account. Jiwatlal Pratapsey's munim also told the Income-tax Officer that the appellant was operating all these accounts. At the hearing of this appeal the fact of appellant's operating several of these accounts was admitted, although the explanation was that the appellant did so in his brother's absence. There is no proof whatever that the appellant's brothers, Hariram and Vishandas, were doing business with M/s Jiwatlal Pratapsey. Therefore, the irresistible conclusion is that these different accounts were those of the appellant himself, being maintained in the names of his different relations.

23. As stated before, M/s Jiwatlal Pratapsey's books show a loss of Rs. 4,650 in respect of cotton dealings in the appellant's own name. But they also disclose a net profit of Rs. 27,275 in the account of Shrichand Nandlal and Rs. 3,730 in that of V. Beharilal, amounting in all to Rs. 31,005. But the Income-tax Officer, while estimating the cotton profits at this figure, does not appear to have taken into account the loss of Rs. 4,650 incurred by the appellant in respect of transactions done in his own name. It is not suggested that the profits could be estimated at a higher figure so as to ignore the loss in question. On the Income-tax Officer's own estimate, therefore, the net profit in respect of cotton business would be Rs. 26,355.

24. Coming to the share business, the Income-tax Officer estimated the total profit in the accounts of S. D. Chandani and others at

Rs. 20,000. This was doubtless a pure estimate, because M/s Jiwatlal Pratapsey were not able to produce their subsidiary books which were necessary for a more precise ascertainment. The S. D. Chandani account itself showed that the profits made by the appellant in that account in respect of share business amounted to something over Rs. 8,000. Further, the turnover in Chandani account amounted to over 2 lacs of rupees. In our opinion therefore, the estimate was not at all arbitrary or excessive. The broker's books also showed that the appellant was also doing ready business in shares the profits from which it was difficult to ascertain. In a business like this there may be an interval between the purchases and sales of shares, and also the purchases might have been made through different brokers. Therefore, in the absence of proper books of account it was impossible for the Income-tax Officer to ascertain the profit even approximately. He therefore estimated it at Rs. 5,000 which estimate, in our opinion, is fair.

25. Next, on enquiry the Income-tax Officer discovered that the appellant had done business, chiefly in silver, with a number of persons, the addresses of most of whom he could not find out. As far as could be ascertained, the appellant earned profit of Rs. 988 from C. Parekh & Co., Rs. 1,324 from Bhagwandas Motilal; Rs. 1,763 from Ganpatlal Madhavji; and Rs. 133 from V. Kasalchand, amounting in all to Rs. 4,188.

26. Thus the appellant's total business income which the Income-tax Officer computed, partly by estimates and mostly on reference to the books of the various parties with whom the appellant dealt, aggregated to Rs. 1,72,604. Out of this amount the appellant was obviously entitled to be allowed a total loss of Rs. 64,245 admitted and verified by the Income-tax Officer as shown above. But it is contended on behalf of the appellant that he must be allowed two more items of alleged losses, namely, Rs. 23,000 paid to Vishandas and Rs. 5,000 in respect of Indore cotton. Vishandas is appellant's brother, and in the accounting year was living in the family home at Shikarpur, Sind. There was nothing whatsoever to indicate that the appellant had done any business with him. When questioned by the Income-tax Officer on the point, Vishandas admitted that he had no proof to support the story. From his pass-book of the Bank of India, Bullion Exchange Branch, it appears that the total credits amounted to hardly Rs. 13,000 and the debits Rs. 8,000, in the accounting year. He told the Income-tax Officer that he had received two cheques from his brother, on 27th July 1936 and 5th August 1936, for Rs. 9,403 and Rs. 3,500, respectively. But the amounts of these cheques do not appear to have been credited into the bank account. M/s Karanjawalla & Co., who were the appellant's

Income-tax representatives in these proceedings made no allusion to the payment of Rs. 23,000 to Vishandas in their letter, dated 11th August 1938, in which they detailed the amounts received from and paid to various parties. The appellant produced a written declaration of his brother before the Appellate Assistant Commissioner to the effect that he had been paid a sum of Rs. 23,000 but it was both vague and lacking in detail. Therefore, a broad allegation of payment to a brother for losses did not at all carry conviction, and the Appellate Assistant Commissioner was perfectly right in disallowing the item. Similar is the case with the alleged loss in Indore cotton. The appellant told the Income-tax Officer that he had paid the loss to 'miscellaneous parties' whom, however, he could not name. Before the Appellate Assistant Commissioner he told a somewhat different story that the alleged loss was from business done with the Kantilal Mehta, a representative of Radhakisan Kanmal firm. But he added at the same time that the firm had been dissolved, and that he was not able to produce any proof in support of the loss. In these circumstances, this item too, in our opinion, was rightly disallowed. We therefore think the appellant's business income should have been estimated at Rs. 1,08,359. Out of this amount a further item of Rs. 1,200 was allowed to the appellant on account of expenses. Thus the net total business income comes to Rs. 1,07,159. The Income-tax Officer computed the income at Rs. 1,50,000 on an estimated basis. He tried to support this estimate remarking that his enquiries had disclosed that the appellant had earned as much profit in 1936-37. But speculation business has its own vicissitudes, and it would be unfair to adopt such a basis as the Income-tax Officer has done, especially in view of the detailed investigation which he carried out. At any rate, the details of his own estimate do not take the figure of income higher than that just reached by us with the assistance of his own notes.

27. Coming to the second main source of income, *i.e.*, from dividends, the Income-tax Officer estimated it at Rs. 15,000 which included Rs. 3,000 as "wife's income". Except the business done by the appellant in the name of his wife in the S. D. Chandani account, the respondent is unable to point out to us any source from which the appellant's wife might have earned the income in question. In this respect, therefore, we are constrained to hold that the Income-tax Officer's estimate was more or less a surmise. There is, however, sufficient indication on the record to support his estimate of the appellant's own dividend income of Rs. 12,000. In his assessment order, the Income-tax Officer has traced the growth of the appellant's investments in shares and securities. In the accounting year in question, he collected not less

than Rs. 6,500 through Bank of India and Rs. 1,000 through Parekh & Co. The total dividend collected by the appellant was ascertained to be Rs. 8,717. It was also admitted before us that he had received dividends through other parties in respect of his shares standing in their names. Considering also that he bought Rs. 35,000 worth Tata deferred shares, we do not think that the Income-tax Officer's estimate of dividend at Rs. 12,000 was either unfair or improper.

28. The last two items of the income are interest and income from property which the Income-tax Officer calculated at Rs. 1,000 and Rs. 600, respectively. There is no substantial contest in regard to the latter. But we think that the Income-tax Officer over-estimated the interest income. The several bank books examined by him disclosed that the appellant had earned not more than Rs. 148 as interest and bonus in the accounting year. It therefore seems to us that the estimate of Rs. 1,000 under this head was excessive.

29. In the view that we have taken the appellant's assessable income comes to Rs. 1,19,907 as below :—

| | Rs. |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------|
| (i) Profit as per appellant's statement verified by the Income-tax Officer ... | 1,17,061 |
| (ii) Cotton business profits earned from M/s Jiwatlal Pratapsey in the names of Srichand Nandlal and V. Beharilal, less loss in the appellant's own name (in Teji-Mandi) ... | 26,355 |
| (iii) Share profit, on ready and forward, from M/s Jiwatlal Pratapsey in the names of S. D. Chandani and others estimated ... | 20,000 |
| (iv) Share profit, in ready in on name from M/s Jiwatlal Pratapsey estimated ... | 5,000 |
| (v) Profit from business from persons undisclosed, but discovered by the Income-tax Officer :—Parekh & Co., Bhagvandas Motilal; Ganpatlal Madhavji, V. Kasalchand, and others ... | 4,188 |
| | <hr/> 1,72,604 |
| Less :—Loss admitted and verified by the Income-tax Officer ... | 64,245 |
| | <hr/> 1,08,359 |
| Less :—Expenses allowed by the Income-tax Officer ... | 1,200 |
| | <hr/> 1,07,159 |
| Add :— | |
| Dividend ... | 12,000 |
| Interest ... | 148 |
| Property income ... | 600 |
| | <hr/> Total ... 1,19,907 |

30. On a careful consideration of all the contentions and the material proof in this case, we partially allow Regular Assessment appeal R.A.A. No. 13/Bombay of 1940-41 by reducing the appellant's assessable income from Rs. 1,66,600 to Rs. 1,19,907, and order that the

assessment be modified accordingly. Rest of this appeal, as well as the other appeal, 27 C.A.A. No. 1/Bombay of 1940-41, have no substance, and are dismissed."

On the application of the assessee under Section 66 (1) of the Indian Income-tax Act (XI of 1922), the Appellate Tribunal (Bombay Branch) referred the case to the Bombay High Court:—

STATEMENT OF CASE.

"We are respectfully making this reference on a petition of the assessee, Mr. Dayaldas Khushiram, under Section 66 (1) of the Indian Income-tax Act, 1922 (as amended on 1st April, 1939). The petition is marked Ex. A in the appended list. In paragraph 5 of the petition the assessee has formulated not less than 12 questions as questions of law arising out of our appellate judgment in the assessee's appeal, Regular Assessment Appeal No. 13 Bombay—of 1940-41. But while arguing the petition, the learned counsel confined himself only to four, namely, Nos. 4, 7, 8 and 10. As a matter of fact most of the rest appear to be parts of the main question involved in the four. As regards question No. 12 which is vaguely expressed, the learned counsel thought that it was not necessary to submit it to their Lordships. We think, however, that it involves a very important point that would vitally affect this reference, as will appear presently. Briefly speaking, the assessee questions the validity of a supplementary assessment made upon him under Section 34 of the Income-tax Act, 1922, for the charge year 1937-38.

2. The Commissioner of Income-tax, Central, who is the respondent has filed his written answer, Ex. B, in which he has formulated only two questions.

3. The assessee is taking his assessment for a second time to the High Court. Once before he did so by a petition under Section 45 of the Specific Relief Act, and the case is reported as *Dayaldas Kushiram v. Commissioner of Income-tax, Central*—1940 INCOME-TAX REPORTS, page 139.

4. The facts of this case and the vicissitudes through which it passed are sufficiently set out in our appellate judgment. We are reluctant to burden this reference with their repetition, and shall, therefore, confine ourselves only to narrating such undisputed facts as will help to understand the questions that we propose to submit.

5. An assessment was made upon the assessee for the charge year 1937-38 on an estimated income of Rs. 25,000 by the Income-tax Officer, C Ward, Section II, Bombay, who was admittedly the Income-tax Officer appointed for the local area in which the assessee was doing

business, and who could, therefore, legally make the assessment under Section 64 (1) of the Income-tax Act. It was what is known as the 'best judgment assessment' and was made under Section 23 (4) of the Act on account of the assessee's failure to declare his income in the return that he had submitted. Copy of the assessment order is Ex. C.

6. Towards the end of October, 1938, the Commissioner of Income-tax, Bombay, Sind and Baluchistan, appointed a set of Income-tax Officers designated Income-tax Officers, Special Provincial Circle, for the purpose of levying assessments in important cases that might be assigned to them. One of these officers was Mr. V. T. Shah to whom the Commissioner made over the assessee's case by an order, dated October 31, 1938. The assessment that was then due to be made was for the year 1938-39. On going through the assessment record the Income-tax Officer thought that the assessee had been under-assessed for the year 1937-38, and, accordingly, started proceedings of re-assessment by means of a notice, dated December 20, 1938, under Section 34 of the Act. It was served upon the assessee on the following day. In compliance with its requirements the assessee filed a fresh return declaring an income of Rs. 25,000 upon which he had been originally assessed, with a remark to the effect that that was all his income from the different sources indicated in the notice. Certain correspondence followed between the assessee and the Income-tax Officer which is not material, except one letter, dated February 20, 1939, which the assessee wrote questioning the jurisdiction of the Income-tax Officer, Special Provincial Circle, to make his assessments. We shall refer to the action taken upon this letter presently.

7. The proceedings remained without making much progress, till April 1, 1939, when the amended Act came into force. Section 5 of the Act came to be re-written. Sub-section (2) of that section empowered the Central Government to appoint a Commissioner of Income-tax without reference to area, and to the exclusion of any Commissioner appointed for any area, to exercise the functions of a Commissioner of Income-tax in respect of cases or classes of cases assigned to him by the Central Board of Revenue. In exercise of these powers, the Central Government appointed Mr. Bird as Commissioner of Income-tax, Central, with effect from April 1, 1939. Shortly afterwards, Mr. Bird organized six sections called Sections I to VI, Central, and, in exercise of his powers under sub-section (5) of Section 5 of the amended Act, appointed a set of Income-tax Officers called Income-tax Officers, Central, to deal with cases assigned by him. Mr. V. T. Shah who was doing duty as Income-tax Officer, Special Provincial Circle, came to be appointed to the Central, and was assigned Section II.

Among the assessments made over to him was the assessee's supplementary assessment for 1937-38 and the assessments for 1938-39 and 1939-40 which last had then become due. In the present reference we are concerned with the supplementary assessment alone which Mr. V. T. Shah completed on June 19, 1940, assessing the assessee on a total income of Rs. 1,66,600. This time, too, the assessment was made on an estimate according to the best judgment of the Income-tax Officer, under Section 23 (4) of the Act, on account of the assessee's default in complying with a notice under Section 22 (4) of the Act requiring him to produce certain documents and papers. A copy of the assessment order is Ex. D. The assessee applied to the Income-tax Officer under Section 27 of the Act to set aside the best judgment assessment, but the Officer declined to do so. He took successive appeals from that order, but failed. We are not concerned with this part of the case in the present reference.

8. The assessee took the assessment in appeal to the Appellate Assistant Commissioner who confirmed it. A copy of his order is Ex. E.

9. Finally, he appealed to the Appellate Tribunal. We held that the assessee had been rightly assessed under Section 23 (4), but reduced the estimated income to Rs. 1,19,907. A copy of our judgment is marked Ex. F*.

10. Here it may be mentioned that neither the Income-tax Officer, Special Provincial Circle, nor the Income-tax Officer, Section II, Central, was an Income-tax Officer appointed for the local area in which the assessee was doing business. Section 5 (4) of the Income-tax Act (before amendment) which in all respects corresponds to Section 5 (5) of the amended Act empowers a Commissioner of Income-tax to distribute and allocate the work among his Income-tax Officers. It was under Section 5 (4) that the Commissioner of Income-tax, Bombay, Sind and Baluchistan, and, under Section 5 (5) the Commissioner of Income-tax, Central, purported to act in making over the assessee's case to those Income-tax Officers respectively.

11. Shortly after the re-assessment proceedings were initiated by Mr. V. T. Shah, Income-tax Officer, Special Provincial Circle, the assessee wrote to him the letter alluded to before questioning the Officer's jurisdiction to make the assessments on the ground just stated, and asked that the point might be referred to the Commissioner, Bombay, Sind and Baluchistan, under Section 64 (3) of the Act. On such a reference being made, the Commissioner passed an order, dated March 9, 1939, marked Ex. G which runs thus:—

*The Judgment of the Appellate Tribunal is printed at p. 69 *supra*.

"A question of proper place of assessment having arisen under Section 64 (3) of the Income-tax Act, the assessment of the assessee for the year 1938-39 is made over to the Income-tax Officer, C Ward, Section II, Bombay."

Here it may be noted that this order contains no reference to the supplementary assessment now in dispute.

12. Another order of the Commissioner which may be mentioned in this place is dated April 1, 1939, Ex. H. It runs as follows:—

"Under Section 5 (5) of the Indian Income-tax Act as amended, the Income-tax Officer, C Ward, Section II, Bombay, is hereby appointed to hold charge of the duties of the Income-tax Officers of the Special Provincial Circle for Income-tax, Bombay, in addition to his own for the purposes of assessments in the cases of assesseees shown in the accompanying statement for the years mentioned against them."

One of the cases alluded to in this order is the re-assessment now in dispute. This was apparently an administrative order of posting of officers, but a point is attempted to be made out of it, as will appear later in course of this reference.

13. In about June, 1939, the assessee once again raised the same point before the Income-tax Officer, Section II, Central, on similar grounds, and asked for fresh reference to the Commissioner, Central, under Section 64 (3) of the Act. After hearing the assessee on the reference, Mr. Bird, who was then Commissioner of Income-tax, Central, made an order dated July 12, 1939, marked Ex. J., the concluding portion of which is as follows:—

"I, therefore, hold that the case has been properly allotted to Section II, Central, and that the Income-tax Officer in charge of that Section is correctly vested with the powers to levy assessments in the case for the years 1937-38 (supplementary), 1938-39 and 1939-40."

14. Aggrieved by this order, the assessee petitioned to the High Court, Bombay, under Section 45 of the Specific Relief Act, praying that the Commissioner of Income-tax, Central, and the Income-tax Officer, Section II, Central, might be directed to forbear from proceeding with his assessment for want of jurisdiction. Their Lordships heard and disposed of the rule holding that the Commissioner had no power under Section 5 (5) of the amended Act to make over the assessee's case to the Income-tax Officer, Section II, Central; and that the latter had equally no power to levy the assessment. The main ground upon which their Lordships' decision was based was that under Section 64 (1) of the Act an assessee had an indefeasible right to be assessed by an Income-tax Officer appointed for the local area in which he did business, and that the Income-tax Officer, Section II, Central, not being such

an Officer, had no power to levy the assessment, in the absence of any amendment in Section 64 (1) of the Act corresponding to the changes made in Section 5.

15. Their Lordships' decision was pronounced on December 15, 1939. On 30th following the Governor-General, in exercise of his powers under Section 42 of the Government of India Act, 1935, promulgated an Ordinance No. IX of 1939. Briefly speaking it validated the proceedings of a Commissioner of Income-tax in respect of cases of assessments assigned to him under sub-section (2) of Section 5 by the Central Board of Revenue, and those of the Income-tax Officers charged by him with levying assessments in such cases under Section 5 of the Act, by enacting that sub-sections (1) and (2) of Section 64 shall not apply and shall be deemed never to have at any time applied to such cases but the assessment of such persons whether the proceedings were taken before or after 1st April, 1939, shall be made by the Income-tax Officer for the time being charged with the functions of making such assessment by the Commissioner to whom he is subordinate. A copy of the Ordinance* is Ex. K.

16. It appears that one Eruchshaw Sorabjee Marker who was being similarly assessed had made a similar petition to the High Court and obtained a similar judgment on the same date. After the promulgation of the Ordinance he made an application to the High Court (Miscellaneous Application No. 115 of 1939, Ordinary Original Civil Jurisdiction) praying to take action against the Commissioner of Income-tax, Central, and the Income-tax Officer concerned for contempt in disobeying their Lordships' judgment of 15th December preceding. In this case the effect of the Ordinance upon their judgment came to be considered by their Lordships, and they held that the Ordinance in question overrode their judgment. Beaumont, C.J., observed that while the High Court judgment directed the Income-tax Officer to forbear from making the assessment, the Ordinance directed him to make it. Admittedly the judgment in Marker's contempt petition affected the one that the assessee had obtained.

17. But the assessee did not rest there and raised the point of jurisdiction once again before the Appellate Assistant Commissioner in his regular assessment appeal. The Assistant Commissioner disposed of the contention with a brief remark—"There can be no manner of doubt that the Ordinance validated the proceedings and rendered the High Court's judgment of 17th December, 1939, nugatory."

18. The point was revived before us in appeal. It will appear from their Lordships' judgment in the assessee's petition under the

* See (1940) 8 I.T.R. Notes 3.

Specific Relief Act that the assessment proceedings which they held to have been taken without jurisdiction were those taken by the Income-tax authorities, Central, from April 1, 1939, under the amended Act. Further, Section 2 of the Ordinance excluded the action taken by the Commissioner of Income-tax, Central, in cases made over to him, under Section 5 (2), and, in turn, entrusted by him to his Income-tax Officers under Section 5 (5) of the amended Act, from the application of Section 64 (1) of the Income-tax Act. From this the learned counsel argued, in the first place, that the Ordinance in question overrode the High Court's judgment as far as it affected such proceedings alone, and not those that had been taken before advent of the amended Act. In other words, he tried to restrict the validating effect of the Ordinance to the assessment proceedings taken on and from April 1, 1939. But such a position was difficult to sustain in view of the concluding portion of Section 2 of the Ordinance which expressly included within its scope proceedings taken before that date under the pre-amendment Act and continued under the amended Act. The learned counsel attempted to tide over this difficulty contending that the re-assessment proceedings commenced with the notice under Section 34, dated December 20, 1938, by the Income-tax Officer, Special Provincial Circle, were invalid inasmuch as that officer was not the proper officer to make assessment or supplementary assessment under Section 64 (1) of the Act; and that the Ordinance would have no effect upon such proceedings even if they came to be continued from April 1, 1939, under the amended Act. In other words, the substance of his contention was that the Ordinance would not help to validate the assessment proceedings by reason only of their being continued under the amended Act from April 1, 1939, if they were initially invalid. He further contended that as a matter of fact there was no continuance of the earlier proceedings from April 1, 1939, onwards, so that there were no such proceedings of re-assessment in the hands of the Income-tax Officer, Section II, Central, such as could be validated by the Ordinance. The department's answer to the first contention was that the concluding portion of Section 2 of the Ordinance governed a case of this kind, and validated the proceedings of re-assessment irrespective of their initial invalidity, provided that the assessment was made by the Income-tax Officer, Section II, Central, as directed by the Ordinance. As regards the second point, they maintained that the proceedings initiated in December 1938, did as a matter of fact continue till the assessment was completed by the Income-tax Officer in question.

19. On a consideration of these several points we reached the following conclusions :—

(i) That the proceedings of re-assessment initiated by the Income-tax Officer, Special Provincial Circle, by means of the notice, dated December 20, 1938, were invalid, being taken by an officer who was not an Income-tax Officer competent to make the assessment under Section 64 (1) of the Act.

(ii) That the proceedings remained in the charge of the Income-tax Officer, Special Provincial Circle, till April 1, 1939, and that thereafter he continued to hold charge of the same proceedings under a fresh designation of Income-tax Officer, Section II, Central, so that there was a continuity of the entire proceedings till the re-assessment was completed.

(iii) That the concluding portion of Section 2 of the Ordinance governed the assessee's case and validated his re-assessment, notwithstanding that the proceedings were initially invalid for want of jurisdiction.

We have detailed our reasons for these conclusions in paragraphs 14, 15 and 16 of our judgment to which we respectfully invite their Lordships' attention.

20. Before leaving this part of the case, we feel bound to bring to the notice of their Lordships a development which the assessee has made in the present petition in his case on the second of the three points stated above. His contention in appeal before us was that on a reference being made under Section 64 (3) of the Act at his instance, the Commissioner of Income-tax, Bombay, Sind and Baluchistan, withdrew his assessments from the Income-tax Officer, Special Provincial Circle, and made them over to the proper officer, namely, Income-tax Officer, C Ward, Section II, Bombay, and thus terminated the proceedings commenced without jurisdiction, so that no re-assessment proceedings remained to be made over to the Income-tax Officer, Section II, Central, on and from April, 1939, in the absence of a fresh notice under Section 34 of the Act. In this connection, the learned counsel relied upon two orders of the Commissioner of Income-tax, Bombay, Sind and Baluchistan, dated March 9, 1939, and April 1, 1939, respectively. We have reproduced these two orders in paras 11 and 12 of this reference, and have dealt with them in paras 10 and 16 of our judgment. In our opinion, neither of these two orders had the effect of withdrawing the supplementary assessment in contest from the Income-tax Officer, Special Provincial Circle. Speaking more particularly of the second order, it only appointed the Income-tax Officer, C Ward, Section II, Bombay, to hold charge of the Provincial Circle, and, with it, the supplementary assessment of the assessee. We held that such an order did not imply a withdrawal of the supplementary assessment from the Special Provincial Circle. In the present petition,

the assessee has tried to put an altogether different construction upon that order with the assistance of an affidavit which is stated to have been sworn by Mr. Bird, Commissioner of Income-tax, Central, on October 4, 1939, and filed in the High Court's record of the assessee's petition under Section 45 of the Specific Relief Act. Para. 4 (3) of the assessee's petition purports to reproduce its contents. Mr. Bird is stated to have sworn that the order of the Commissioner of Income-tax, Bombay, Sind and Baluchistan, dated April 1, 1939, placing the Income-tax Officer, C Ward, Section II, Bombay, in charge of the duties of the Income-tax Officer, Special Provincial Circle, in addition to his own, was made for reasons of convenience so as to allot the assessment of the petitioner under Section 34 to the officer who was also seised of the case for the assessment year 1938-39. From this it is argued that the order in question had the effect of withdrawing the supplementary assessment from the Income-tax Officer, Special Provincial Circle, and transferring it to the proper Income-tax Officer, C Ward, Section II, Bombay. For more than one reason we are unable to take into consideration this new development in this part of the assessee's case. In the first place, a copy of Mr. Bird's affidavit was not produced in the assessment proceedings at any stage, nor was it offered in appeal before us. It was not even referred to in course of the counsel's arguments. The assessee is now trying to introduce an altogether new fact which was not before us when we heard the appeal, and we do not think that he can be permitted to do so at the present stage. Further, it will have to be borne in mind that the order of April 1, 1939, was made by the Commissioner of Income-tax, Bombay, Sind and Baluchistan, who should have been the best person to speak of its meaning. Mr. Bird who made the affidavit six months later was an altogether different officer, being a Commissioner of Income-tax, Central. That being so, his statement can only be regarded as his own view of the order passed by another officer. Primarily, we have to look to the language of the order which, in our opinion, admits no such construction as Mr. Bird came to put upon it long afterwards. No further light is possible to be thrown on its meaning, inasmuch as we understand that the officer who held the post of Commissioner of Income-tax, Bombay, Sind and Baluchistan, on April 1, 1939, has since retired from service, and Mr. Bird, who was Commissioner of Income-tax, Central, is dead.

21. As far as we can see these are the several points raised in questions Nos. 4, 7, 8 and 10 in para. 5 of the assessee's petition. In our opinion, only one question can be formulated out of them for reference to their Lordships.

22. But before doing so, we think that it is necessary to raise three more that arise out of the contentions taken by the department in appeal before us, and which, they contend, will preclude consideration of the question raised by the assessee. An important part of the case for the department was that a Commissioner of Income-tax is the sole authority under the Act to decide the question as to the place of assessment of an assessee, i.e., a question regarding the jurisdiction of an Income-tax Officer to make assessment in the case of an assessee; and that an order that may be passed by the Commissioner under Section 64 (3) of the Act, such as the one dated July 12, 1939, is a final order so that an appellate authority constituted under the Income-tax Act has no power to entertain any such question in appeal. It was further contended that even the absence of such an order would make no difference to an assessee's case, inasmuch as his only remedy would be a reference to the Commissioner, under Section 64 (3) of the Act. We accepted the department's contention on both these points following two decided authorities of the Allahabad High Court—*Seth Kanhaiyalal v. Commissioner of Income-tax, C.P. and U.P.*¹, and *Seth Kanhaiyalal Goenka, In re*²—and held that the point such as the one raised by the assessee could not be entertained in appeal. We respectfully invite their Lordships' attention to paras. 10, 11 and 12 of our judgment in which we have dealt with this part of the case.

23. Therefore, one of the questions that we propose to submit in addition to the one raised in the assessee's petition is whether the order, dated July 12, 1939, passed by the Commissioner of Income-tax, Central, under Section 64 (3) of the Act can be questioned in an appeal to the Income-tax Appellate Tribunal. The assessee has vaguely raised this point in question No. 12 in paragraph 5 of his petition. But while arguing the petition, the learned counsel said that he would not ask for a reference on that point. Expressed in his own words his argument was : "You may have no power to entertain a question of jurisdiction in appeal. But the High Court does possess such a power because it did exercise that power in the assessee's petition under Section 45 of the Specific Relief Act."

24. But such an argument appears to side-track another important point arising out of the question. Under Section 66 (1) of the Indian Income-tax Act (as amended in 1939), the Appellate Tribunal, on a petition of the assessee, is required to refer to the High Court any question of law arising out of the appellate order passed by it. If however the Tribunal has no power to entertain a point of jurisdiction such as the one raised in this case it will not be a point arising out of our

(1) (1937) 5 I.T.R. 739.

(2) (1941) 9 I.T.R. 25.

appellate judgment, although the assessee might have put it in his memo of appeal. This view is also supported by the two decided authorities that we have just referred to. Doubtless, we dealt with the question of jurisdiction on the merits also, but that was with a view to dispose of the case on all the points raised before us. That will make no difference to the position of the assessee and give him a right to ask us to refer the question to the High Court.

25. We, therefore, respectfully submit the following questions for their Lordships' decision :—

Questions referred :

- (1) Whether the order dated July 12, 1939, passed by the Commissioner of Income-tax, Central, under Section 64 (3) of the Income-tax Act, 1922, deciding the place of assessment of the petitioner, can be the subject of an appeal to the Income-tax Appellate Tribunal under Section 33 of the Act ?
- (2) Whether the Income-tax Appellate Tribunal has power to entertain in appeal a question as to the place of assessment of an assessee, even in the absence of an order of a Commissioner of Income-tax under Section 64 (3) of the Act ?
- (3) If either of the first two questions is answered in the negative, whether a question as to the place of assessment put in an appeal to the Tribunal is a question of law arising out of its appellate judgment, so as to be subject matter of a reference to the High Court under Section 66 (1) of the Indian Income-tax Act, 1922 ?
- (4) Whether the Governor-General's Ordinance No. IX of 1939 (later incorporated in Section 64 of the Income-tax Act by an amendment of 1940) has the effect of regularising or validating the proceedings of re-assessment of the petitioner for the charge year 1937-38, irrespective of whether they were initiated by the Income-tax Officer, Special Provincial Circle, without jurisdiction to make the assessment."

Coltman with Taraporewalla, for the assessee.

M. C. Setalvad with G. N. Joshi, for the Commissioner.

JUDGMENT.

BEAUMONT, C. J.—In this case the Appellate Tribunal, Bombay, has submitted four questions to this Court under section 66 (1) of the Income-tax Act. The questions arise in these circumstances,

The assessment upon the assessee for the year 1937-38 was made on the 8th of October 1937 by the Income-tax Officer, C Ward, Section II, which was one of the divisions of Bombay City for the purposes of the Income-tax Act made by the Commissioner of Income-tax, Bombay, Sind and Baluchistan, under Section 5 of the Act before the amendment of 1939. On the 21st of October 1938 the Commissioner of Income-tax, Bombay, Sind and Baluchistan, created a Special Provincial Circle, for which he appointed certain Income-tax Officers to exercise jurisdiction throughout the limits of his own jurisdiction, that is Bombay, Sind and Baluchistan, in respect of certain cases transferred to them, and on the 31st of October he transferred to that Special Provincial Circle the assessee's case. The Special Provincial Circle Officer on the 20th of December 1938 served a notice under Section 34 of the Act alleging that part of the assessee's income for the year 1937-38 had escaped assessment. Thereafter that officer had before him the assessment of the assessee for 1938-39, and the re-assessment for 1937-38. On the 9th of March 1939 the Commissioner of Income-tax, Bombay, Sind and Baluchistan, seems to have felt some doubt about the validity of his order transferring the assessee's case to the Special Provincial Circle, and he therefore purported to make an order under Section 64 (3) of the Act that the assessment in the cases of the assessee shown in the accompanying statement for the year shown against each of them should be made by the Income-tax Officer, C Ward, Section II, and the accompanying statement contained the name of the assessee, and against it the year 1938-39. So the assessment for 1938-39 was retransferred to the Income-tax Officer, C Ward, but nothing was said about the re-assessment of 1937-38 under the notice under Section 34. I should have supposed that that omission was due to the view of the Commissioner that the notice under Section 34 was invalid and a nullity so that there was nothing to transfer in respect to that, but that view is rather negatived by the subsequent order made by the Commissioner on the 1st of April 1939 under the Act as then amended whereby under Section 5 (5) of the amended Act the Income-tax Officer, C Ward, Section II, was appointed to hold charge of the duties of the Income-tax Officers of the Special Provincial Circle for Income-tax, Bombay, in addition to his own for the purposes of assessments in the cases of assessee shown in the accompanying statement for the years mentioned against them which statement contained the name of the assessee and against it the year 1937-38 under Section 34. So that the re-assessment was purported to be covered by that order. Subsequently the Commissioner of Income-tax, Central, who had been appointed by the Central Board of Revenue under the amended Act, made various

orders including one of 12th July 1939 which are discussed in my judgment in *Dayaldas Kushiram v. Commissioner of Income-tax*¹, which dealt with the present assessee's case and it is sufficient to say that the Commissioner, Central, purported to assign the assessee's case to one Mr. Shah who was one of the Income-tax Officers appointed by the Central Commissioner without reference to area. In December 1939 this Court gave the decision to which I have just referred the effect of which was that it was not competent to the Income-tax authorities to transfer the case of the assessee to an Income-tax Officer appointed without reference to area since he was entitled to be assessed by the local officer under Section 64 (1) which had not been amended. As a consequence of that decision the Governor-General promulgated an Ordinance on the 28th of December 1939 to which I will refer in detail when I come to answer question (4).

In those circumstances the questions raised are first :

“ Whether the order dated July 12, 1939, passed by the Commissioner of Income-tax, Central, under Section 64 (3) of the Income-tax Act, 1922, deciding the place of assessment of the petitioner can be the subject of an appeal to the Income-tax Appellate Tribunal under Section 33 of the Act? ”

That question seems to be founded in error because when one looks at the order of the 12th of July 1939 which as I have mentioned is one of the orders made by the Commissioner of Income-tax, Central, the Commissioner states that it is clear beyond doubt that no question arises for determination within the meaning of Section 64 (3). The order which the Commissioner passed that the case of the assessee had been properly allotted to the Income-tax Officer, Section II, Central, was apparently based on his view of the terms of Section 5 (2) of the Income-tax Act ; so that the order of the 12th of July was not in fact made under Section 64 (3). Moreover there appears this difficulty that the Governor-General's Ordinance directs that the provisions of sub-section (1) and sub-section (2) of Section 64 of the Indian Income-tax Act are to be deemed not to apply and never to have applied to the present assessee and as Section 64 (3) is confined to deciding any question arising under the section as to the place of assessment I do not see how any order under Section 64 (3) could affect the assessee. I think therefore that question (1) does not arise and need not be answered.

The second question is :

“ Whether the Income-tax Appellate Tribunal has power to entertain in appeal a question as to the place of assessment of an assessee,

(1) (1940) 8 I.T.R. 139 ; 42 Bom. L. R. 414.

even in the absence of an order of a Commissioner of Income-tax under Section 64 (3) of the Act?"

To my mind that question is also based in error. The Income-tax Act does not determine the place of assessment. What it does is to determine the officer who is to have power to assess and in some cases it does so by reference to locality but I apprehend that an appeal would be not against an order of the Commissioner as to the place of assessment, but against the order of assessment of the Income-tax Officer. I apprehend that the sort of question which the Tribunal had in mind is whether when an assessee is assessed by an Income-tax Officer and it is suggested that the Income-tax Officer had no jurisdiction to make the assessment because an order purporting to give him such jurisdiction made under Section 64 (3) was wrongly made, a right of appeal would lie. When a question of that sort arises we will decide it to the best of our ability but at present it does not arise. I will only observe that such a question could probably not be answered merely by looking at Section 30 and observing that under that section no right of appeal against an order under Section 64 (3) is conferred since the appeal could probably be not against an order made under Section 64 (3) but against the consequences following from such order. However I am satisfied that we ought not to answer a question which does not arise.

The third question is based on the assumption that either of the first two questions is answered in the negative and as we have not answered the first two questions either in the affirmative or in the negative the third question does not arise.

The fourth question is the only one which arises and it is in these terms :

"Whether the Governor-General's Ordinance No IX of 1939 (later incorporated in Section 64 of the Income-tax Act by an amendment of 1940) has the effect of regularising or validating the proceedings of re-assessment of the petitioner for the charge year 1937-38, irrespective of whether they were initiated by the Income-tax Officer, Special Provincial Circle, without jurisdiction to make the assessment."

The position under the orders to which I have referred seems to me to be that the Income-tax Officer, Special Provincial Circle, was validly appointed under Section 5 (4) of the Act before amendment. His appointment was confined to the area over which the Commissioner who appointed him had jurisdiction and in my view was valid but as held by this Court the assignment to that officer of the assessee's case was invalid, by reason of the provisions of Section 64. Apart from any difficulty created by Section 64, it is in my opinion clear that the assessee's case was subsequently assigned by the Commissioner,

Central, to the Central Officer Mr. Shah who purported to continue the re-assessment of 1937-38. The question is whether he could do so and that depends on the terms of the Ordinance.

Section 2 of the Ordinance provides so far as material that the provisions of sub-section (1) and sub-section (2) of Section 64 of the Indian Income-tax Act, 1922, shall not apply and shall be deemed never at any time to have applied to any assessee on whom a re-assessment for the purposes of that Act is being made in the course of any case or class of cases in respect of which a Commissioner of Income-tax appointed without reference to area under sub-section (2) of Section 5 of the Act is exercising the functions of a Commissioner of Income-tax under the Act. This Ordinance is retrospective in character and must undoubtedly be construed strictly and no case should be brought within it which is not fairly within its language.

It is argued by Mr. Coltman that you cannot say that a re-assessment of the assessee was being made in the course of a case in respect of which the Central Commissioner was exercising the functions of a Commissioner because the re-assessment was never validly started. It was however validly started in my view apart from the difficulty arising under Section 64. The difficulty which Mr. Coltman points out seems to me to be removed so far as the assessee is concerned by the latter part of Section 3 of the Ordinance which provides: "No assessment made in accordance with Section 2 before the commencement of this Ordinance, and no proceedings taken in the course of or for the purposes of so making an assessment before the commencement of this Ordinance shall be or continue to be invalid by reason of anything contained in Section 64 of the Indian Income-tax Act, 1922." To my mind the only invalidity in this re-assessment arose under Section 64. Apart from that section, I think all the orders made by the two Income-tax Commissioners concerned were valid and it seems to me that Sections 2 and 3 of the Ordinance have removed the invalidity of the orders made prior to the passing of the Ordinance so far as they relate to the assessee.

In my opinion therefore we must answer the fourth question in the affirmative.

No order as to costs.

Negative Certificate under Section 205 of the Government of India Act to be granted.

KANIA, J.—The relevant facts, orders and sections of the Act and the Ordinance have been summarised in the judgment just delivered by the learned Chief Justice.

As regards the first question submitted for the Court's opinion in the reference it is sufficient to state that no order under Section 64 (3) has been made by the Commissioner as expressly stated in his order dated 12th of July 1939. It cannot therefore be said that the question arises for decision in this case.

The second question is framed generally. In respect of questions of jurisdiction the point may arise under Section 64 (3) or otherwise and the jurisdiction of the Tribunal to entertain disputed questions of jurisdiction of the particular Income-tax Officer will depend on the proper construction of the relevant sections of the Income-tax Act. It is not proper for the Court on different hypotheses to give different answers without the particular facts being clearly put before it. In that view I do not think that the second question arises here and is proper to be decided by the Court under the circumstances of the case.

Question (3) need not be answered, because it follows questions (1) and (2).

As regards question (4), shortly put, the only question is whether the notice dated the 20th of December 1938 was invalid on the ground that the assessee had acquired a right under Section 64 (1) or it was invalid on the ground that the appointment of the Officer "Special Provincial Circle" was *ultra vires*. If it was invalid on the ground of Section 64 the same is validated by reason of the Ordinance and the wide terms thereof making its operation retrospective. Section 2 (a) read with the words at the end of that section and the words in the latter half of Section 3 clearly validate any proceeding in the matter of an assessment or re-assessment pending before an Income-tax Officer, Central, at the moment when the Ordinance was issued if the alleged invalidity was on the ground of Section 64 of the Income-tax Act. If the legality of the notice dated the 20th of December 1938 is challenged on the ground that the appointment of the Income-tax Officer, Special Provincial Circle, was invalid, the same has to be considered apart from the Ordinance under Section 5 of the Income-tax Act before its amendment in 1939. Section 5 (4) in terms authorised the Commissioner of Income-tax to appoint Income-tax Officers for certain areas and also in respect of certain cases which I read as confined to those areas. The order made by the Commissioner in this case dated the 21st of October 1938 in terms created the post of an Income-tax Officer, Special Provincial Circle, within the area of Bombay Province, Sind and Baluchistan. Apart from the considerations brought to bear on reading Section 64, I do not think the appointment as such was invalid under Section 5 (4). The previous decision of the Court, which has been much relied upon, does not help the petitioner because the decision of the Court was only

that the assessee having acquired a right to be assessed under Section 64 by the particular officer and that as an officer with the designation covered by the words of Section 64 existed, his right cannot be taken away by a later amendment of Section 5 of the Income-tax Act without a corresponding amendment of Section 64. That case did not purport and did not decide anything beyond this. Therefore the assessee's contention raised in question (4) must fail. The answer therefore is as stated in the judgment of the learned Chief Justice.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

MESSRS. GOVINDRAM SEKSARIA, *In re.*

BEAUMONT, C. J., and KANIA, J.

September 30, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922 AFTER AMENDMENT OF 1939)
SECS. 5, 22 (2), (4), 28 (4), 27, 30, 43, 64—INCOME-TAX OFFICER—APPOINTMENT—ASSISTANT INCOME-TAX OFFICER APPOINTED TO PERFORM FUNCTIONS OF INCOME-TAX OFFICER—WHETHER ENTITLED TO MAKE ASSESSMENT ORDER—APPOINTMENT AS AGENT UNDER SECTION 43—WHETHER HOLDS GOOD FOR SUBSEQUENT YEARS—WHETHER CAN BE DISPUTED IN RE-ASSESSMENT FOR SAME YEAR—BEST JUDGMENT ASSESSMENT—FAILURE TO COMPLY WITH TERMS OF NOTICE—WHETHER ASSESSEE PREVENTED FROM SUFFICIENT CAUSE—RIGHT OF APPEAL AGAINST BEST JUDGMENT ASSESSMENT—WHETHER EXTENDS TO CASES PENDING ON 1ST APRIL 1939 BUT WHICH WERE ASSESSED SUBSEQUENTLY—ABOLITION OF SPECIAL CIRCLE AND TRANSFER OF CASE TO INCOME-TAX OFFICER, SECTION II, CENTRAL—VALIDITY OF NOTICES—ORDINANCE No. (IX OF 1939).

Where G, an Assistant Income-tax Officer, was appointed to perform the functions of an Income-tax Officer and was posted to hold charge of a section vice P, an Income-tax Officer who was granted leave, and G continued to draw the salary of an Assistant Income-tax Officer and signed the assessment order as Assistant Income-tax Officer :

*Held, that G was not a duly appointed Income-tax Officer and he was therefore not entitled in law to make the assessment order.**

BEAUMONT, C. J.—*Income-tax Officers have to perform very responsible duties and an assessee is entitled to say that he can only be assessed*

* The difficulty caused by this decision in the administration of Income-tax law has been removed by the passing of the Income-tax Proceedings Validity Ordinance, 1943, printed *supra* and published in the Gazette of India dated January 16, 1943.

by somebody who is on the relevant date in the grade of Income-tax Officer and that he cannot be assessed by somebody who is not in that grade but is merely appointed to perform the function of an officer in that grade.

The assesseees were assessed for the year 1935-36 under Section 43 as statutory agents and they paid the tax: Held, that it was not open to them to assert in the re-assessment under Section 34 for that year that they were not agents of the principal.

BEAUMONT, C.J.—*There are obvious difficulties in holding that an appointment of an agent for one year will hold good for subsequent years.*

KANIA, J.—*The scheme of the Income-tax Act is that the assessment for each year is self contained and therefore the contention that once a notice is served on the party and he is held to be an agent such decision is good for all times to come unless the party himself moves and takes steps to get that decision set aside is not correct.*

The Income-tax Officer, Central, served on the assesseees on 8th August 1939 a notice under Section 22 (4) to produce certain books. The assesseees challenged the Income-tax Officer's jurisdiction and the High Court on 15th December 1939 upheld the assesseees' contention. On 30th December the Governor-General passed an Ordinance which overruled the decision of the High Court. From 30th December to 2nd January 1940 the Income-tax Office was closed and on 3rd January the Income-tax Officer assessed the assesseees under Section 23 (4) for failure to comply with the terms of the notice. The assesseees applied under Section 27 to have the assessment cancelled:

Held, (1) that the assesseees were prevented by sufficient cause from complying with the terms of the notice, inasmuch as after 30th December when the order for producing the books was validated, the assesseees were not given reasonable time in which to produce their books;

(2) that in making the assessment under Section 23 (4) the Income-tax Officer did not exercise his judgment honestly and without caprice;

(3) that the assesseees were entitled to file an appeal against the assessment order under Section 23 (4).

BEAUMONT, C.J.—*It is quite impossible to say that an Income-tax Officer in every assessment pending on 1st April 1939 had a vested right to insist that if he should make an assessment under Section 23 (4) it must be final.*

COLONIAL SUGAR REFINING CO. v. IRVING ([1905] A.C. 369), DELHI CLOTH AND GENERAL MILLS CO. v. COMMISSIONER OF INCOME-TAX, DELHI

[1927] (54 I.A. 421) and **SAKEENA BIBI AND OTHERS v. C. STEPHENS** [1926] (4 Rang. 221) *distinguished*.

Held also, *on the facts, following DAYALDAS KHUSHIRAM v. COMMISSIONER OF INCOME-TAX, CENTRAL (BOMBAY)* [1943] (11 L.T.R. 67) (1) *that the notice issued under Sections 34 and 22 (2) on the 19th March 1937 did not cease to be valid and effective in law by reason of the abolition of the Special Circle and the transfer of the assessee's case to the Income-tax Officer, Section I (Central) ;*

(2) *that although the notice under Section 22 (4) dated 8th August 1939 was originally invalid on the ground that it was not issued by the Income-tax Officer of the area in which the assessee's place of business was situate, it was subsequently validated by Ordinance No. IX of 1939.*

Cases referred to :—

Colonial Sugar Refining Co. v. Irving [1905] A.C. 369.

Dayaldas Khushiram v. Commissioner of Income-tax, Central (Bombay) (1943) 11 L.T.R. 67.

Delhi Cloth and General Mills Co. v. Commissioner of Income-tax, Delhi (1927) 54 I.A. 421 ; A.I.R. 1927 P.C. 242 ; 9 Lah. 284.

Sakeena Bibi and Others v. Stephens (1926) 4 Rang. 221 ; A.I.R. 1926 Rang. 205 ; 97 I.C. 1025.

Case referred to the High Court by the Commissioner of Income-tax (Central), Bombay, under Section 66 (2) of the Indian Income-tax Act (XI of 1922) for the decision of the questions of law mentioned in para 11 of the Commissioner's Statement of Case : (Income-tax Reference No. 8 of 1942).

STATEMENT OF CASE.

“ My LORDS,

1. Under Section 66 (2) of the Indian Income-tax Act (hereinafter referred to as the Act) and at the instance of Messrs. Govindram Seksaria (hereinafter called the assessee) in their capacity as Agent, under the provisions of Section 43 of the Act, to one Mahavirprasad Vishwanath of Navalgaadh, I beg to submit to your Lordships the questions of law set forth in paragraph 10 below which arise out of the two orders of the Appellate Assistant Commissioner, A Range, Bombay, dated 9th May 1940, upholding the order of the Income-tax Officer under Section 27 refusing to reopen the assessment under Section 27 of the Act and confirming the assessment order passed by the Income-tax Officer, Section I (Central), in respect of the assessment of the assessee as Agent to Mahavirprasad Vishwanath for the assessment for 1935-36 based on the accounting period Sambat 1990.

2. **Facts of the Case.**—The assessee is a registered firm carrying on business in Bombay, on their own account as well as on account of certain constituents residing in places outside British India, such as Navalgaadh, as in the present case, and are known to have been doing

speculative business in cotton and other commodities, on behalf of Mahavirprasad Vishwanath of Navalgad, since 1932. A notice under Section 43 was issued to the assesseees on the 12th December, 1932, whereby the Income-tax Officer concerned intimated his intention to treat the assesseees as the agents of the non-resident, Mahavirprasad Vishwanath of Navalgad, and invited the assesseees to state their objection, if any, by a specific date. A copy of the said notice is hereto annexed as Exhibit 'A'. As there was no response to the said notice, the Income-tax Officer issued a notice under Section 22 (2) calling upon the assesseees to submit their Return of income for 1932-33 in their capacity as Agents of Mahavirprasad Vishwanath. The assesseees submitted their Return by describing themselves as such Agents and the Income-tax Officer concerned completed the assessment for 1932-33 by treating the assesseees as such Agents. No separate notice under Section 43 was issued in any of the subsequent years in respect of the subsequent years assessments. In each subsequent year, the assesseees filed a Return as Agents to Mahavirprasad Vishwanath, pursuant to the notice under Section 22 (2) issued by the Income-tax Officer concerned for filing such Returns, and were assessed as such Agents and paid the tax.

3. For the year 1935-36 the assesseees were assessed as Agents for Mahavirprasad Vishwanath by the Income-tax Officer, Special Circle, by an assessment order dated the 25th March 1936 (copy whereof is annexed as Exhibit 'B' hereto) under Section 23 (1) of the Act, on a total income of Rs. 21,711 in respect of which the amount of tax demanded and paid by the assessee firm was Rs. 2,506-9-0. The return submitted by the assesseees for 1935-36 had been accepted as correct by the Income-tax Officer, Special Circle, without asking for the production of any books of account or any other documents, and the assessment was made under Section 23 (1) of the Act.

4. After the assessment was made, certain information came to the knowledge of the Income-tax Officer, Special Circle, which gave him reason to believe that the income of the non-resident had partially escaped assessment for 1935-36, and he therefore issued a notice to them under Sections 22 (2) and 34 of the Act, on the 19th March, 1937, calling upon them to furnish a fresh Return of income for 1935-36 within thirty days of the receipt of the notice. The assesseees did not submit any Return within the time. No action was taken by the Income-tax Officer until March 1939. When these proceedings under Section 34 were pending with the Income-tax Officer, Special Circle, who was an officer subordinate to the Commissioner of Income-tax, Bombay Presidency, Sind and Baluchistan, the case was assigned to the Commissioner of Income-tax (Central) by an order dated the 18th April, 1939,

issued by the Central Board of Revenue, under Section 5 (2) of the Income-tax Act. By an order dated the 27th April, 1939, the Commissioner of Income-tax (Central) directed the Income-tax Officer, Section I (Central), who was subordinate to him to perform the functions of an Income-tax Officer in respect of the assesseees as Agents, by name. Thereafter, the Income-tax Officer, Section I (Central), continued the pending proceedings under Section 34 which had been started by the Income-tax Officer, Special Circle, on the 19th March, 1937. As the Return of income called for by the aforesaid notice dated the 19th March, 1937, issued by the Income-tax Officer, Special Circle, had not been furnished, a reminder asking for the early submission of the Return was sent to the assesseees by the Income-tax Officer, Section I (Central), on 26th July, 1939. In spite of the said reminder, no Return was furnished by them. In this connection, it may be stated that in connection with the separate case relating to their own personal assessment the assesseees had raised in June 1939 the question of jurisdiction of the Central Income-tax Officer to make assessments and that a similar question was raised by another assessee named Dayaldas Kushiram and that the question was decided by the High Court of Bombay on the 15th December 1939.

5. On the 8th August, 1939, the Income-tax Officer, Section I (Central), issued a notice under Section 22 (4), calling upon the assesseees to produce before him on the 14th August, 1939, the Cash Book, Ledger, Journal, Soda Book and Soda Khata of Messrs. Govindram Seksaria for the year 1930-31 (Maru) showing the Khata and transactions of the non-resident during the said year. On the 12th August, 1939, the assesseees asked for an adjournment, and the case was accordingly adjourned to the 19th August, 1939. On the 18th August, 1939, the assesseees wrote and asked to be supplied with three blank forms of Returns of income to enable them to submit the same duly filled in, and also with true copies of such of the Returns of income for 1935-36, 1936-37 and 1937-38 as may have been filled in and filed by them previously in the Income-tax Office. They undertook to pay the copying charges for the latter. The blank forms of Returns of income asked for by the assesseees were supplied to them on the 24th August, 1939. On the same day a chalan was sent to them for the copying charges in respect of their application for copies of their earlier Returns of income.

6. As after this date there was no response of any kind whatsoever from the assesseees either to the notice issued under Sections 22 (2) and 34 or to the notice issued under Section 22 (4) of the Act, Mr. Gondalia, the Income-tax Officer, Section I (Central), passed an order on the 3rd

January, 1940 (copy whereof is annexed hereto as Exhibit 'C') under Section 23 (4), assessing them on a total income of Rs. 2,21,712 in respect of which a total amount of Rs. 57,109 was demanded as the net tax due from them after giving allowance for the tax already paid.

The original assessment order dated 25th March, 1936 (Exhibit 'B') was on a total income of Rs. 21,711. The supplementary assessment order dated 3rd January, 1940 (Exhibit 'C') was on a total income of Rs. 2,21,712. The difference between the two figures was due to the fact that an item of Rs. 2,00,000 which appeared in the account of Mahavirprasad in the books of Messrs. Govindram Seksaria was treated in the supplementary assessment as the profit of Mahavirprasad Vishwanath. The fresh assessment was based on the notes of examination which were recorded in the case of the personal assessment of the firm of Messrs. Govindram Seksaria. An extract of the said notes of examination and of the marginal notes recorded thereon by the Income-tax Officer concerned is annexed hereto as Exhibit 'D'.

7. The assesseees applied to the Income-tax Officer, Section I (Central), to re-open the assessment under Section 27 of the Act and the latter, after hearing them, passed an order declining to do so. A copy of the said order is hereto annexed and marked 'E'. The assesseees then filed two appeals to the Appellate Assistant Commissioner, A-Range, Bombay; first against the Income-tax Officer's orders under Section 27 refusing to re-open the assessment and secondly, against the quantum of the assessment. Copies of the said two appeals are hereto annexed and marked 'F' and 'G' respectively.

8. Appellate Assistant Commissioner, A-Range, passed two orders, both dated the 9th May, 1940, dismissing both the said appeals, by two separate orders. Copies of the said orders are annexed hereto as Exhibits 'H' and 'I' respectively.

9. The assesseees have now applied to me for making a reference to the Honourable High Court, under Section 66 (2) of the Act, in respect of certain questions of law alleged to arise from the said order of the Appellate Assistant Commissioner. Hereto annexed and marked 'J' is a copy of the application under Section 66 (2) submitted by the assesseees.

10. Correspondence has taken place between me and the Solicitors of the assesseees in regard to the facts to be stated in the Letter of Reference and the questions of law which arise for decision. The said correspondence is annexed hereto and marked collectively 'K'.

11. The only questions of law which, in my opinion, arise for decision by your Lordships out of the said two orders are as follows :—

Questions of Law for Decision.

1. Whether the notice issued under Sections 34 and 22 (2) on the 19th March, 1937, ceased to be valid and effective in law by reason of the abolition of the Special Circle and the transfer of the assessee's case to the Income-tax Officer, Section I (Central).

2. Whether the notice under Section 22 (4) dated 8th August, 1939, not having been issued by the Income-tax Officer of the area in which the assessee's place of business was situate, the said notice and the proceedings based on it are valid in law.

3. Whether Mr. G. H. Gondalia who made the assessment order dated the 3rd January, 1940, was a duly appointed Income-tax Officer entitled in law to make the said order.

4. Whether, in the absence of a fresh notice under Section 43 in respect of the assessment year 1935-36, the assessment levied on the assessee as Agents for Mahavirprasad Vishwanath is valid in law.

5. Whether there was evidence before the Income-tax Officer on which he could have come to the conclusion that the assessee had failed to show that they had been prevented by sufficient cause from complying with the terms of the said notices under Section 22 (2) and Section 22 (4).

6. Whether the assessee was entitled to file an appeal to the Appellate Assistant Commissioner against the assessment order dated 3rd January, 1940, under Section 23 (4) of the Act.

7. Whether, in the event of question 6 being answered in the negative, any questions of law alleged to arise out of the order of the Appellate Assistant Commissioner dated 9th May, 1940, in regard to the said assessment order under Section 23 (4), can be decided by this Hon'ble Court.

8. Whether, in making the assessment under Section 23 (4), the Income-tax Officer exercised his judgment and acted honestly and without caprice.

12. *Opinion of the Commissioner.*—As required by the provisions of Section 66 (2) of the Act, I submit my opinion on each of the above questions, for your Lordships' consideration :—

Question (1).—The assessee's case regarding the notice issued by the Income-tax Officer, Special Circle, on 19th March 1937 under Sections 22 (2) and 34 is that it became invalid on the abolition of the Special Circle, or, at any rate, from the date of assignment of the assessee's case to the Income-tax Officer, Section I (Central), on 27th April 1939. It is submitted that this contention is not sound, as there is nothing in the Act which makes the renewal of a notice obligatory every time a case is transferred from the jurisdiction of one Income-tax

Officer to another. The transfer of a case would clearly include also a transfer of pending proceedings. This point was considered by your Lordships in *Dayaldas Kushiram v. Commissioner of Income-tax (Central)*¹, and it was held that the notice issued under Section 34 by the Income-tax Officer, Special Provincial Circle, in respect of a case subsequently transferred to the Central Branch, continued to be valid. I submit, therefore, that this question should be answered in the negative.

Question (2).—As regards the notice under Section 22 (4) issued on 8th August, 1939, by the Income-tax Officer, Section I (Central), the assessee contends that all proceedings taken by that Income-tax Officer were invalid on the principles laid down by this Honourable Court in *Dayaldas Kushiram v. Commissioner of Income-tax (Central)*.¹ In the said case it was decided that an assessee who was under the jurisdiction of the Income-tax Officer of a particular area under Section 64 of the Act, had a right to be assessed by the Income-tax Officer of that area and could not be assessed by an Income-tax Officer who was appointed to an area larger than, though comprising, the above-mentioned smaller area. These contentions of the assessee, however, ignore later legislation comprised in Ordinance IX of 1939 dated the 30th December, 1939, and Sections 6 and 9 of the Act XII of 1940. It is submitted that the effect of the said legislation clearly is to validate the said notice and the said proceedings from their inception.

In the circumstances, therefore, I submit that the answer to this question should be in the affirmative.

Question (3).—The contention of the assessee is that Mr. Gondalia who passed the assessment order dated the 3rd January, 1940, was at that time only an Assistant Income-tax Officer, and being not one of the authorities specified in Section 5 (1) of the Act, was not competent to discharge the functions of an Income-tax Officer under the Act. The material facts in this connection are that Mr. Gondalia was, up to the 26th September, 1939, an Assistant Income-tax Officer, Bombay City, under the Commissioner of Income-tax, Bombay Presidency, Sind and Baluchistan. By order No. 376, dated the 27th September, 1939, he was appointed an Income-tax Officer by the Commissioner of Income-tax (Central). This order runs as follows:—

“Mr. G. H. Gondalia, B. Com., G.D.A., A.S.A.A., Assistant Income-tax Officer, Bombay City, is hereby appointed, with effect from 27th September, 1939, forenoon to perform the functions of an Income-tax Officer and is posted to hold charge of Section I (Central) *vice* Mr. H. B. Parekh, B.A., granted leave. He will take over charge from Mr. S. B. Athalye, M.A., LL.B.”

In another order dated 25th September 1939, the Commissioner of Income-tax (Central) had granted leave to Mr. H. B. Parekh, the then Income-tax Officer of Section I (Central), and had further directed that (a) "On the expiry of the leave Mr. Parekh's services will be placed at the disposal of the Commissioner of Income-tax, Bombay Presidency, Sind and Baluchistan" and (b) "until further orders, Mr. S. B. Athalye, Income-tax Officer, Section IV (Central), will hold charge of Section I (Central) in addition to his own duties." This explains why Mr. Gondalia was directed in the above mentioned order No. 376 to take over charge from Mr. Athalye, though, in the same order, he was appointed Income-tax Officer *vice* Mr. Parekh. Order No. 376 no doubt describes Mr. Gondalia as an Assistant Income-tax Officer, but this reference is to the designation of the office which he held, in the office of the Commissioner of Income-tax, Bombay Presidency, Sind and Baluchistan up to the date of his appointment as Income-tax Officer, Section I (Central). The order, after describing him as an Assistant Income-tax Officer, goes on to appoint him to perform the functions of an Income-tax Officer. It is submitted that this can only mean that, being an Assistant Income-tax Officer up to the date of his appointment in the Central Branch, Mr. Gondalia is, from and after that date, appointed to be an Income-tax Officer in Section I (Central). The use of the word "appointed" in the order clearly indicates that what is being effected by the order is a fresh appointment, and not merely the conferring of additional powers on a person already appointed. The assessee further contend that the Commissioner of Income-tax (Central) was not competent to appoint Income-tax Officers under the provisions of the Income-tax Act, and that the alleged appointment by him of Mr. Gondalia as an Income-tax Officer does not constitute him a duly appointed Income-tax Officer. In regard to the question of the competency of the Commissioner of Income-tax (Central) to appoint Income-tax Officers, it is submitted that Section 5 (3) of the Act confers the power to appoint Income-tax Officers on the Central Government. By reason of Section 4-A of the General Clauses Act (X of 1897) the reference to the Central Government in Section 5 (2) of the Act would include a reference to such person as the Central Government may direct. By Notification No. F. 99/36 dated the 14th April, 1937, a copy whereof is annexed as Exhibit "L", the Governor-General-in-Council has directed that any officer subordinate to him who was authorised by any existing Indian law in force immediately before the 1st April, 1937, to make appointments in civil posts under the Crown, is authorised to make the said appointments in the like manner as before the said date. Section 7 of the Government of

India Act provides that the executive authority of the Federation is to be exercised by the Governor-General. The directions contained in the Notification dated the 14th April 1937, would therefore be a direction given by the Central Government. Immediately before the 1st April, 1937, the Commissioner of Income-tax was empowered by Section 5 (4) of the Indian Income-tax Act, as it stood on that date, to appoint Income-tax Officers. It is submitted, therefore, that by reason of the above-mentioned section of the General Clauses Act read with the above-mentioned Notification of the Governor-General of the 14th April, 1937, the Commissioner of Income-tax retained the power of appointing Income-tax Officers after the 1st April 1937. There can, therefore, be no doubt that the Commissioner of Income-tax (Central) was competent to appoint Mr. Gondalia as an Income-tax Officer under the Act.

For the reasons stated above, I submit that your Lordships be pleased to answer question (3) in the affirmative.

Question (4).—Under Section 43 of the Act as it stood before its amendment in 1939, which applies in the present case, any person employed by or on behalf of a person residing out of British India, or having any business connection with such person, or through whom such person is in receipt of any income, profits or gains, upon whom the Income-tax Officer has caused a notice to be served of his intention of treating him as the agent of the non-resident person, shall, for all the purposes of this Act, be deemed to be such agent. It is further provided by the section that no person shall be deemed to be the agent of a non-resident person unless he has had an opportunity of being heard by the Income-tax Officer as to his liability. It is submitted that the section does not require the steps mentioned therein to be taken in respect of the assessment of each year. If a person has been served with a notice under that section and has, after giving him an opportunity of being heard, been deemed to be an agent of a non-resident person and has thereafter acquiesced from year to year in being treated as an agent and has been assessed as such agent it would, it is submitted, be unnecessary to serve him with a notice under that section for every subsequent year. In this connection I beg to rely on the case of *Commissioner of Income-tax, Punjab v. Nawalkishore Kharaitilal*¹ decided by the Privy Council and the decision of the Lahore High Court in *Nawalkishore Kharaitilal v. Commissioner of Income-tax*.² If once a notice under Section 43 has been issued to a party and he has been declared to be an agent of a non-resident party, no separate notice under Section 43 need be issued to the resident

(1) (1938) 6 I.T.R. 61

(2) (1934) 4 I.T.C. 451; 2 I.T.R. 350.

principal for each successive year of assessment; it will suffice if the Income-tax Officer, by serving him with a notice under Section 22 (2) or 22 (4), gives him the necessary opportunity to represent his objection, if he has any, to his being treated as an agent. In the present case, it is clear that the assesseees were treated as Mahavirprasad Vishwanath's agents since 1932, and that they had since then acquiesced in that position from year to year. In fact, even in respect of the main assessment for 1935-36 they accepted the assessment order and paid the tax in their capacity as agents. Also, even after they had been served with notices under Sections 34 and 22 (2) in respect of the supplementary assessment for 1935-36 now in question, they wrote a letter on 18th August 1939, to the Income-tax Officer, Section I (Central), describing themselves as Agents to Mahavirprasad Vishwanath, and asking for blank forms of Returns of income to be submitted to the Income-tax Officer in pursuance of the above-mentioned notices. It is therefore abundantly clear that the assesseees had always accepted, and did accept, in respect of the 1935-36 supplementary assessment, the position of Agents to Mahavirprasad Vishwanath. It is also clear that they had ample opportunity of being heard by the Income-tax Officer, Section I (Central), as to their liability to be treated as Agents. I submit, therefore, that your Lordships should answer the question (4) in the affirmative.

Question (5).—The question whether the assesseees were prevented by sufficient cause from complying with the terms of the notices issued to them is entirely a question of fact. The only question of law that can be said to arise from the order of the Appellate Assistant Commissioner refusing to set aside the Income-tax Officer's order under Section 27 is whether there is any evidence upon which the Appellate Assistant Commissioner could find that there was not sufficient cause to prevent the assesseees from submitting the Return or producing the accounts in response to the notices issued. It has been held by the Rangoon High Court in *Abdul Bari Choudhury v. Commissioner of Income-tax, Burma*¹, that if there was such evidence before the Appellate Assistant Commissioner, his order cannot be interfered with. Under Section 22 (4) of the Act, the fact of failure to comply with a notice under Section 22 (2) or 22 (4) makes it compulsory on the Income-tax Officer to make an assessment to the best of his judgment. It has been held by the Privy Council in *Commissioner of Income-tax, C. P. and U. P. v. Laxminarain Badridas*² that, under Section 27, unless the Income-tax Officer is satisfied that the assessee had not a reasonable opportunity to comply, or was prevented by sufficient cause from

(1) (1931) I.L.R. 9 Rang. 281.

(2) (1937) 5 I.T.R. 176.

complying with the notices issued to him, the assessment must stand. Whether there was actually sufficient cause for failure to comply with the notices in question is itself, however, a question of fact (vide *Commissioner of Income-tax, C. P. and U. P. v. Laxminarain Badridas*¹); the only question of law that arises is whether there was any evidence on which the Income-tax Officer could possibly come to the conclusion that there was no sufficient cause. The Income-tax Officer is the sole person to judge the question; and his conclusion on the question of the adequacy of the reason for non-compliance cannot be questioned as a point of law (vide *Commissioner of Income-tax, C. P. and U. P. v. Laxminarain Badridas*¹).

The assesseees have not explained, at any stage of the proceedings before the Appellate Assistant Commissioner, or before my predecessor, in the course of the hearing of their application under Section 66 (2), why they did not submit the Return of income called for in the notice issued by the Income-tax Officer, Special Circle, on the 19th March 1937. They admit that they applied for copies of the Return forms on the 18th August 1939 but they do not say why, on these forms being supplied to them on the 24th August, 1939, they failed to submit their Return of income. In any case, no explanation whatsoever was given to the Income-tax Officer to account for their failure to submit their Return of income, and the Income-tax Officer cannot therefore be said to have acted capriciously or dishonestly in coming to the conclusion that no sufficient cause existed for this failure, for the obvious reason this if there had been such cause, it would have been the easiest thing for the assesseees to explain that to him.

As regards the production of the account books in response to the notice under Section 22 (4), the assesseees have tried to explain their failure in this respect, primarily on the ground that the practice in the Income-tax Department has been for the Income-tax Officers to be content with the books of account produced by the principal in his own assessment case, even in matters relating to the assessment of such principal as the agent of non-resident parties. Without admitting for a moment that this alleged practice, even if it existed, is a sufficient excuse for an assessee to ignore the notices served on him by an Income-tax Officer, it might, perhaps, be useful to correct a fundamental error underlying the assesseees' explanation. The correct position is that in assessments under Section 43 the books of account are required to be called for separately only in such cases as where these accounts are desired to be examined again, namely, after their examination in connection with the assessment of the principal;

but, in a case like the present one, where the assessment proceedings were reopened under Section 34, and where, obviously, the accuracy of the original Return of income submitted by the party was open to question, it was clearly necessary for the Income-tax Officer to examine the relevant books of account again. In such cases the books are specifically called for by a separate notice and, unless the assessee has some interest in concealing the true facts at this stage, the books are usually produced. There is no foundation at all, therefore, for the contention of the assessee that the alleged past practice in the Income-tax Department in Bombay justified their non-compliance with the Income-tax Officer's notice in the present case. The notice should have been complied with, without question, even if the assessee thought that the Income-tax Officer could have got all the information which he wanted from the records already available to him. The Act allows no discretion to the assessee in this matter and the Income-tax Officer's orders have to be complied with, irrespective of what the assessee thinks about the necessity for them or otherwise. The assessee not only defaulted in the matter of producing their account books, but also failed to give any reasonable explanation to the Income-tax Officer for their default. In the circumstances, it cannot be said that the Income-tax Officer acted capriciously or dishonestly in coming to the conclusion that the assessee did not have sufficient cause for their failure to produce their accounts.

It must also be emphasised that even the mistaken assumption of the assessee which has been discussed in the foregoing paragraph would apply to only just one out of the many books and documents they were asked to produce by the notice under Section 22 (4) dated the 9th August 1939, *viz.*, the Ledger. The notice covered certain other books and documents as Cash Book, Journal, Soda Book and Soda Khata, which were also required to be examined in detail. The assessee did not furnish any explanation to the Income-tax Officer for not producing these, and has not furnished any up till now.

Even if the assessee contends that a portion of the books required by the Income-tax Officer was produced during their old assessment, and that such production constitutes partial compliance with the Section 22 (4) notice, I submit that the language of Section 23 (4) makes it quite clear that if the assessee fails to comply with *all* the terms of the notice issued under that section, the Income-tax Officer should make a best judgment assessment. A partial default (even if it is assumed, for the sake of argument, that it is partial in this case) involves the same consequences under Section 23 (4) as a total default. I rely

in this connection on the case reported in *Mohan Lal Hardeo Das v. Commissioner of Income-tax*¹.

In all circumstances, therefore, it is my humble opinion that the only decision that your Lordships can arrive at is that the Income-tax Officer had material before him on which he could come to the conclusion that the assessee had failed to show that they had been prevented by sufficient cause from complying with the terms of the said notices and that question No. (5) should be answered in the affirmative.

Question (6).—Under Section 30 as it stood before the amendment of it in 1939, no appeal lay to the Assistant Commissioner in respect of an assessment under Section 23 (4). It is submitted that the right of appeal is a substantive right and not a matter of procedure and that the assessee has not this right in respect of the assessment for the year 1935-36 in respect of which proceedings had been started in 1937, even though the actual order of assessment was made after the amendment of the Act. This question should therefore, in my opinion, be answered in the negative.

Question (7).—It is submitted that if no appeal was competent in law, the fact that an appeal was entertained by the Assistant Commissioner and an order passed therein cannot confer any rights on the assessee. There is, it is submitted, no valid and competent order of the Assistant Commissioner out of which any questions of law could be said to arise, and in my opinion this question should also be answered in the negative.

Question (8).—The only question of law that can arise in connection with the quantum of an assessment under Section 23 (4) is whether or not the Income-tax Officer exercised his judgment in arriving at the amount assessed by him. Whether or not the amount for which the assessee is assessed is the correct amount on which the assessee should have been assessed is a question of fact and not a question of law. If, therefore, it is reasonably clear that the Income-tax Officer, in making the assessment under Section 23 (4), did not act dishonestly, vindictively or capriciously, it must be assumed that his assessment was, in fact, done according to the best of his judgment, in an honest and judicial manner, and it will not be open to the assessee to agitate the question of the amount of assessment on its merits and contend that the assessment should not have been levied, or that the amount arrived at is incorrect. What has therefore to be examined is the manner in which the Income-tax Officer treated the evidence that was available to him and see whether in arriving at his conclusion, he has acted in a dishonest, vindictive or capricious manner. In the

present case, the Income-tax Officer had called upon the assesseees (a) to file their Return of income, and (b) to produce certain books of account and other documents. Neither the Return nor the books of account, documents, etc., asked for were produced by the assesseees and no explanation whatsoever was given by the assesseees to the Income-tax Officer for their failure to do so. This by itself would have justified the Income-tax Officer suspecting the honesty of the assesseees. He did not, however, permit this suspicion to influence his judgment unduly. He proceeded, on the contrary, in a judicial and impartial manner, to examine what evidence he himself could collect from various sources. He had come to know, for example from certain records pertaining to the assessment of the firm of Messrs. Govindram Seksaria, that a sum of Rs. 2 lakhs had been credited in the firm's books to the account of Mahavirprasad Vishwanath. *Prima facie*, this sum would represent income earned by the assesseees on behalf of the said Mahavirprasad Vishwanath. The Income-tax Officer, however, endeavoured to ascertain the details of the transactions which had led to this credit and what had happened to the amount so credited. He found that on the 8th February, 1934, Mr. Damodar Mahadeo, a munim of the firm of Messrs. Govindram Seksaria, had been paid Rs. 2 lakhs from this account. The Income-tax Officer wanted to verify whether this was corroborated by entries in the Cash Book or in the Ledger of the assesseees. But neither the Cash Book, nor the Ledger, nor the Sauda Bahis, which would have thrown some light on the alleged payment of Rs. 2 lakhs to Mahavirprasad Vishwanath, were produced by the assesseees, though they were called upon to produce them. The Soda Book was of great importance for it would show the transactions entered into by the assesseees on behalf of Mahavirprasad Vishwanath and thus enable the Income-tax Officer to trace the source of the credit of Rs. 2 lakhs. The failure to produce these books helped to confirm the suspicions of the Income-tax Officer that the party was intentionally withholding these important account books and documents with a view to conceal something from him. On top of this, another very suspicious circumstance was that the firm's employee, Mr. Damodar, to whom the amount was alleged to have been handed over, was unable to offer any explanation regarding this large sum of Rs. 2 lakhs. Altogether, there was overwhelming circumstantial evidence before the Income-tax Officer to justify the conclusion that he did arrive at, *viz.*, that the amount of Rs. 2 lakhs known to have been credited to Mahavirprasad Vishwanath's accounts in the books of the firm of Messrs. Govindram Seksaria did represent profits which had escaped assessment. He acted, throughout, in a perfectly judicial manner and

exercised his judgment on such material as was made available to him.

The assessees, in their application, have tried to show that the amount in question was not actually profit earned by them on behalf of the non-resident principal, and they have now produced copies of entries in various books of accounts maintained by them to support their contention. They have also now come forward with their explanation of the various entries, with a view to prove that the Income-tax Officer erred in treating the amount as income. All this, however, is irrelevant to the point referred to your Lordships for decision. I submit that, in the circumstances, the answer to question (8) should be in the affirmative.

13. It is requested that a copy of your Lordships' order may kindly be forwarded to me for necessary action under Section 66 (5) of the Act."

M. C. Setalvad with *G. N. Joshi*, for the Commissioner.

Coltman with *Sir J. B. Kanga*, for the assessees.

JUDGMENT.

BEAUMONT, C.J.—In this case the Commissioner has raised 8 questions, all of which he considers should be answered in his favour.

The facts necessary to be stated by way of introduction are few. The assessment year is the year 1935-36, and the assessees were assessed as the statutory agents, under Section 43 of the Income-tax Act, of one Mahavirprasad Vishwanath. For the assessment year 1932-33 a notice had been given under Section 43, and the assessees had been held to be the statutory agents. No fresh notice was given in subsequent years, but the assessees were assessed as such agents, and in respect of the relevant year 1935-36, they were assessed as statutory agents on the 25th of March 1936, and the tax was paid. On the 19th of March 1937 notice was issued on the assessees under Section 22 (2) and Section 34, alleging that some income for which they were liable as such agents had escaped assessment. The assessment order on that supplementary assessment was made on the 3rd of January 1940 under Section 23 (4), that is to say it was a best judgment assessment.

The first question raised is :

"Whether the notice issued under Sections 34 and 22 (2) on the 19th March 1937 ceased to be valid and effective in law by reason of the abolition of the Special Circle and the transfer of the assessees' case to the Income-tax Officer, Section I (Central)."

It is admitted that, having regard to previous decisions* of this Court, that question must, so far as this Court is concerned, be answered in the negative.

*See *Dayaldas Khushiram v. Commr. of Income-tax, Central (Bom.)* (1943) 11 I.T.R. 67.

The second question is :

“ Whether the notice under Section 22 (4) dated 8th August 1939 not having been issued by the Income-tax Officer of the area in which the assessee's place of business was situate, the said notice and the proceedings based on it are valid in law.”

There, again, it is admitted that, having regard to previous decisions* of this Court, we are bound to hold that the notice, though originally invalid, was validated by the Governor-General's Ordinance of December 1939. I need not, therefore, deal more at length with these questions.

The third question is :

“ Whether Mr. G. H. Gondalia who made the assessment order dated the 3rd January, 1940, was a duly appointed Income-tax Officer entitled in law to make the said order.”

Mr. Gondalia was an Assistant Income-tax Officer on the relevant dates. The Income-tax Act in Section 5 deals with the appointment of Income-tax Officers, but does not mention Assistant Income-tax Officers. They are, we are told, in a lower grade, drawing, naturally, a lower salary, in the Income-tax Office. By an order dated the 27th of September 1939 the Commissioner of Income-tax (Central), that is to say the Commissioner appointed under the amended Income-tax Act without reference to area, passed an order in the following terms : “ Mr. G. H. Gondalia, Assistant Income-tax Officer, Bombay City, is hereby appointed, with effect from 27th September, 1939, forenoon to perform the functions of an Income-tax Officer and is posted to hold charge of Section I (Central), *vice* Mr. H. B. Parekh granted leave. He will take over charge from Mr. S. B. Athalye.” The notification relating to the appointment appeared in the Gazette of India of the 30th September 1939. After a notification that Mr. Parekh, Income-tax Officer, Section I (Central) had been granted leave from the 25th of September 1939, the next notification was in these terms : “ Mr. G. H. Gondalia, Assistant Income-tax Officer, Bombay City, has been appointed to Section I (Central) *vice* Mr. H. B. Parekh, with effect from the 27th of September 1939.”

It is said that the effect of the order of the Commissioner, Central, and the notification in the Gazette, is to appoint Mr. Gondalia an Income-tax Officer to hold charge in the place of Mr. Parekh. But it is noticeable that neither in the order nor in the notification is Mr. Gondalia appointed an Income-tax Officer ; he is appointed to do the work of an Income-tax Officer, but he is described as an Assistant Income-tax Officer ; and I have no doubt that the order was framed in that way, because the authorities wanted to avoid paying Mr. Gondalia

*See *Dayaldas Khushiram v. Commr. of Income-tax, Central (Bom.)* (1943) 11 I.T.R. 67.

salary as an Income-tax Officer. In fact we are told that he continued to draw the pay of an Assistant Income-tax Officer. It is noticeable that he signed the assessment order of the 3rd January 1940, and the order under Section 27 to which I will refer presently, of the 2nd February 1940, as Assistant Income-tax Officer. Merely appointing a man to perform the duties of an office does not amount to a substantive appointment to that office. I apprehend that appointing a District Judge to officiate as a High Court Judge, and to hold office in the place of a High Court Judge proceeding on leave would not by itself constitute the District Judge a High Court Judge, particularly if he continues to draw only the salary of a District Judge. He must be appointed a High Court Judge. Although I have no doubt that an Income-tax Officer can be appointed to act in a temporary vacancy, in my opinion, it is not permissible to appoint somebody, who is not an Income-tax Officer so to act. If the contention of the Commissioner is right, he would be justified in appointing a junior clerk in his office or even the office peon on Rs. 25 per month to perform the functions of an Income-tax Officer. Income-tax Officers have to perform very responsible duties, and I think that an assessee is entitled to say that he can only be assessed by somebody who is on the relevant date in the grade of Income-tax Officer, and that he cannot be assessed by somebody who is not in that grade, but is merely appointed to perform the function of an officer in that grade. Therefore, in my opinion, Mr. Gondalia was not properly appointed.

Mr. Gondalia's appointment was also attacked on the ground that the person appointing him, namely, the Commissioner of Income-tax, (Central), had no power to appoint an Income-tax Officer. It is not necessary to decide that point, as we think that Mr. Gondalia was not in fact appointed. I will only notice that the argument, as I understand it, is that under the Government of India Act the appointment of Income-tax Officers is vested in the Central Government, that although it may be that before the introduction of the Government of India Act, 1935, that power had been delegated to Commissioners, who were all Commissioners appointed with reference to area, and although notification of the Government of India dated the 14th of April 1937, Exhibit L, may have introduced the same provisions after the passing of the Government of India Act, still the Commissioner (Central), appointed without reference to area, was an officer who first came into existence under the Amendment to the Income-tax Act on the 1st of April 1939, and, therefore, it is said that the power to appoint Income-tax Officers was never delegated to him. On the other hand, the Commissioner contends that the delegation was to Commissioners of Income-

tax, and as the Commissioner (Central) was such a Commissioner, he was empowered to appoint Income-tax Officers. As I have said, it is not necessary to say which of those contentions is right, because the point does not arise.

The fourth question is:

“Whether, in the absence of a fresh notice under Section 43 in respect of the assessment year 1935-36, the assessment levied on the assessee as agents for Mahavirprasad Vishwanath is valid in law.”

I think that Mr. Setalvad's argument on behalf of the Commissioner that the larger question, whether notice once given under Section 43 will enure for subsequent years, does not really arise because of the action of the assessee in this particular case. I will only say that I see obvious difficulties in holding that an appointment of an agent for one year will hold good for subsequent years. In order to justify the appointment of an agent under Section 43 the Commissioner has to be satisfied on certain questions of fact, and the assessee has a right to dispute his liability to be deemed the agent. It is obvious, that although an agent may fail in a particular year to resist the claim that he is an agent, circumstances may alter, and in the next year he might be able to resist the claim. However, in this particular case the agents did not dispute their liability to be assessed in respect of the year 1935-36. They were actually assessed, and they paid the tax and it seems to me that that amounts to an admission on their part that in respect of the year 1935-36 they were the agents of the principal for the purposes of Section 43. The re-assessment under Section 34 is a part of the assessment for the year 1935-36, and although the actual re-assessment was not made until the beginning of 1940, the facts necessary to constitute them agents for the re-assessment were the same, and have to be determined for the same date as in the case of the original assessment. I think that in the face of their conduct it is not open to the assessee to assert that for the year 1935-36 they were not the agents of the principal. I have no doubt that the answer to question (4) must be in the affirmative.

Then question (5) is:

“Whether there was evidence before the Income-tax Officer on which he could have come to the conclusion that the assessee had failed to show that they had been prevented by sufficient cause from complying with the terms of the said notices under Section 22 (2) and Section 22 (4).”

Inasmuch as we have held that Mr. Gondalia was not appointed an Income-tax Officer, it may be said that none of the other questions properly arise. But as the case may go further, it is desirable to answer

them. For the purposes of the other questions, I will assume that Mr. Gondalia was properly appointed an Income-tax Officer.

The fifth question really arises in respect of an order made under Section 27. After the re-assessment was made under Section 23 (4), that is as a best judgment assessment, the assessee applied under Section 27 to have the assessment cancelled. In order to establish their right to such an order they have to satisfy the Income-tax Officer that the assessee was prevented by sufficient cause from making the return required by Section 22 (2), or that they did not receive the notice issued under Section 22 (4) or Section 23 (2) or that they had not a reasonable opportunity to comply, or were prevented by sufficient cause from complying, with the terms of the last mentioned notices. The substantial question is whether the assessee was prevented by reasonable cause from complying with the notice for production of their books. Now, the relevant dates are these. On the 27th of April 1939 the Commissioner (Central) assigned the assessee's case to an Income-tax Officer, Central, and on the 15th of June the assessee wrote to that Income-tax Officer challenging his jurisdiction. The objection to jurisdiction was that under Section 64 (1) the assessee was entitled to be assessed by a local Income-tax Officer, and that their case could not be assigned to an Income-tax Officer appointed without reference to area. On the 8th of August the Income-tax Officer served a notice under Section 22 (4) on the assessee requiring them to produce certain books. I think that notice was served on the assessee in their personal capacity and in relation to their personal assessment, but the books could, of course, have been used in relation to their assessment as agents. On the 15th of December 1939 this Court held* in the case of another assessee in exactly the same position as the present assessee, that the contention as to jurisdiction was well founded, and that the assessee in question was not liable to be assessed by an Income-tax Officer, Central. The result was that on that date it was established that the Income-tax Officer, Central, had no business to serve the order which he had served requiring the assessee to produce their books. On the 30th of December the Governor-General promulgated an Ordinance, the effect of which in substance was to overrule the decision of this Court, and the Ordinance was made retrospective. So that, on the 30th of December, for the first time, the order of the 8th of August requiring production of books became valid. Now, it seems to me obvious that the assessee ought to have been given reasonable time in which to produce their books. Up to the 30th of December they were entitled to refuse to produce their books to an officer who had no right to assess.

* *Dayaldas Kushiram v. Commissioner of Income-tax (Central)*, (1940) 8 I.T.R. 139.

them. After the 30th of December they had no right to adopt that attitude. But they ought to have been given reasonable time to produce the books. The Income-tax office was closed from the 30th of December till the 2nd of January, and we are told that the Governor-General's Ordinance was not published in Bombay till the 6th of January. But on the 3rd of January 1940 the Income-tax Officer made his order under Section 23 (4). It seems to me that the assesseees are entitled to say: "We have not had reasonable time to produce our books; in fact we had no time at all since the order requiring us to produce the books became a legal order." I think, therefore, that question (5) must be answered in the negative.

The answer to question (8) very largely depends on the same consideration. That is:

"Whether, in making the assessment under Section 23 (4), the Income-tax Officer exercised his judgment and acted honestly and without caprice."

I think we are bound to say that he did not exercise his judgment honestly and without caprice in making the best judgment assessment without giving any time to the assesseees to produce their books after the order for producing them was validated. I would, therefore, answer question (8) also in the negative.

Then there is question (6), which is:

"Whether the assesseees were entitled to file an appeal to the Appellate Assistant Commissioner against the assessment order dated 3rd January, 1940, under Section 23 (4) of the Act."

The position is that assessments under Section 23 (4) of the Income-tax Act, 1922, were not appealable, until the Act was amended on the 1st of April 1939, when, for the first time, such orders became appealable. Seeing that the order in this case was made on the 3rd of January 1940, I confess that it seems to me rather difficult to see why the order is not appealable. But the Commissioner contends that the right of appeal conferred by the Amendment Act does not extend to any assessment which was pending at that date, and for that he relies on two decision of the Privy Council and one decision of the High Court of Rangoon.

In *Colonial Sugar Refining Company v. Irving*¹ the Privy Council were dealing with a statute which had put an end to appeals to the Privy Council, and they held that a right of appeal is a substantive right, and not a mere matter of procedure, and that in the absence of clear language the statute should be construed as not applying to appeals in suits pending when the statute was passed. The Privy Council held that a man filing a suit is entitled to say: "I have a right to carry my

(1) [1905] A.C. 369.

grievance to the highest tribunal," but that is a substantive right, not lightly to be taken away, and they held that it was not taken away by the statute in that case.

In *Delhi Cloth and General Mills Co. v. Commissioner of Income-tax, Delhi*¹, the Privy Council applied the same principle to a statute granting a right of appeal. They held that a statute granting a right of appeal also dealt with rights, and not procedure, because it put an end to the finality of certain orders, but the Privy Council were then dealing with an order actually been made before the right of appeal was given, and they held that in the absence of clear words the statute should not be construed as giving a right of appeal against a subsisting order.

In *Sakeena Bibi and Others v. C. Stephens*², the principle of that case was applied to a suit pending when the statute was passed, in which no order had been made. Whether that was a legitimate extension of the principle established by the Privy Council, I am not altogether sure. It is one thing to say that a man filing a suit has a vested right to take his case to the highest tribunal then permissible; it is going rather further to say that if and when he obtains a decision from a Court from which at the moment there is no appeal he will have a vested right to treat the order as final, although an appeal is permissible when the order is passed. But, however that may be, I am clearly of opinion that the principle does not apply to an assessment under Section 23 (4) of the Income-tax Act. It is quite impossible, to my mind, to say that an Income-tax Officer in every assessment pending on 1st April 1939 had a vested right to insist that if he should make an assessment under Section 23 (4) it must be final. An Income-tax Officer can only make an assessment under Section 23 (4), where there is default by the assessee, and until the last moment he is not in a position to say whether there will be such default.

I would, therefore, answer question (6) in the affirmative.

Question (7) does not arise.

KANIA, J.—The relevant facts and dates are stated in paragraphs 2 to 9 of the reference, and the material portions have been summarised in the judgment of the learned Chief Justice just delivered. I have nothing to add to the judgment delivered in respect of questions (1) and (2).

In respect of question (3), the question is whether Mr. Gondalia was duly appointed Income-tax Officer, and as such made the order in question. The departmental order, which is recited at page 5 of the reference, only appoints him to perform the functions of an

(1) (1927) L.R. 54 I.A. 421.

(2) (1926) I.L.R. 4 Rang. 221.

Income-tax Officer and posts him to hold charge of Section I (Central) *vice* Mr. H. P. Parekh, granted leave. The first part of that order only clothed him with authority to perform the functions of an Income-tax Officer, which is certainly different from appointing him an Income-tax Officer. The second part, which directs him to hold charge, also does not go to the full length required to make him an Income-tax Officer. To put it at its highest in favour of the Commissioner, Mr. Gondalia by this order held office, where he was to perform the functions of an Income-tax Officer, and was the Assistant Income-tax Officer. It is relevant to refer to the orders made by him in the matter of the assesseees. Both those orders were made and signed by him as "Assistant Income-tax Officer." It is, therefore, clear that although he may be clothed with authority to perform the functions of an Income-tax Officer, in fact in making the orders he did not act as an Income-tax Officer, and the orders in fact made by him, as stated in the orders themselves, were as Assistant Income-tax Officer. It is open to argument that that description was a mistake, but there is no material to show that it was a mistake at all. The notification in the Government Gazette, the terms whereof have been quoted in the judgment of the learned Chief Justice, does not carry the case further. That notification describes Mr. Gondalia as Assistant Income-tax Officer and posts him to Section I (Central), which only means that he will hold charge of that section. But those words do not make him an Income-tax Officer for that section. The further words "*vice* Mr. H. P. Parekh" also, in my opinion, do not take the matter further. It only shows that Mr. Gondalia by virtue of that notification was as if authorised to sit in the chair occupied by Mr. Parekh. In law, as the notification and orders have been worded, in my opinion, it is not proved that Mr. Gondalia was the Income-tax Officer authorized to handle the case of the assesseees and had passed the orders in question in that capacity. I agree, therefore, that the answer to question (3) should be as stated in the judgment of the learned Chief Justice.

A decision on the first part of question (4) is sufficient to answer the question. I agree with the learned Chief Justice in the answer to that for the reasons mentioned in his judgment. The larger argument, which was advanced, is not necessary to be decided, and therefore, I do not propose to express any definite view on that larger question. That contention urged on behalf of the Commissioner is that once a notice is served on the party and he is held to be an agent such decision is good for all times to come, unless the party himself moves and takes steps to get that decision set aside. On a plain reading of Section 43 of the Income-tax Act that view appears to put the burden

altogether on the wrong foot. Under Section 43 before a person can be held liable as agent and proceedings are taken against him, he is entitled to be heard on that question before the Income-tax Officer makes his order. The scheme of the Income-tax Act is that the assessment for each year is self-contained. Bearing that in mind it appears difficult to accept the Commissioner's contention as advanced in the reasons given by him in the reference in respect of question (4).

As regards questions (5) and (8), I have nothing more to add except to emphasize that the proceedings were resisted by the assessee till the 30th of December 1939, and, according to the law of the land as interpreted by the decision of this Court, rightly resisted. If so, the only question for consideration is whether there was default on the part of the assessee thereafter. The time spent in respect of the re-assessment under Section 34 before is not material, because the Income-tax Officer had allowed that time to expire, and from about June 1939 the assessee had taken his stand on the dispute that the Income-tax Officer in question had no jurisdiction to call upon him to furnish the information called for and produce the books mentioned in the notice. If that contention was correct, it is evident that in fact no time at all was given to the assessee to comply with the requisition of the notice, and the conduct of Mr. Gondalia in making the order of the 3rd January 1940 was arbitrary and capricious.

As regards question (6), the three cases cited by Mr. Setalvad, in my opinion, do not support his contention. It is necessary to turn to the words of Section 30 before the Amendment Act of 1939. That section gave a right of appeal to the assessee on the points mentioned thereon. Then there is a proviso, which says that no appeal shall lie in respect of an assessment made under sub-section (4) of Section 23, or under that sub-section read with Section 27. The effect of the amendment in 1939 was *inter alia* to remove this proviso. The question, therefore, is whether in respect of the assessment proceedings, which were pending on the 1st of April 1939, this proviso barred a right of appeal given by the amending Act of 1933. In this connection the words of the proviso, in my opinion, are very clear. They only debar an appeal in respect of an assessment made under that section when that Act was in operation. It does not deal with assessment proceedings pending at the time. Therefore, unless on the date of the Amending Act an assessment order had been made, and in respect of which the taxing authorities, as it is put, had acquired a right to prevent the assessee from making an appeal, no question arises. On the facts it is clear that there was no such assessment made before the 1st of April 1939. Therefore, the words of the proviso do

not debar an appeal to the Assistant Commissioner. In my opinion, therefore, this contention must fail and the question must be answered in the affirmative.

P. C. :—With regard to costs, the Commissioner has succeeded in three questions, two of which, no doubt, were not argued because of previous decisions of this Court, but still they were properly raised, and the assesseees have succeeded in four questions.

We certainly do not propose to lay down any rules which would fetter the discretion of the Court as to costs. But we have to consider the number of questions raised, their difficulty, the amount of evidence involved in dealing with them and the conduct of the parties.

In this case as the Commissioner has failed on the more important questions, we order him to pay one-third of the assesseees' costs.

Certificate to issue that no question under Section 205 of the Government of India Act arises in this case.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

MESSRS. HIRALAL KALYANMAL AMD ANOTHER, *In re.*

BEAUMONT, C. J., and KANIA, J.

September 18, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 4 (1), 10 (2) (ix)—
INCOME—WHETHER INCOME ACCRUES OR ARISES—COMMISSION AGENCY
—SALE ON TERMS *f. o. r.* INDORE TO PERSONS IN BOMBAY—PRICE
RECEIVED THROUGH HUNDIS DRAWN FROM INDORE AND ACCEPTED BY
PURCHASERS IN BOMBAY—HUNDIS COLLECTED IN BOMBAY AND PRO-
CEEDS REMITTED TO INDORE—WHETHER COMMISSION ACCRUES IN
BRITISH INDIA—BUSINESS EXPENDITURE—EXPENSES TO REALISE OUT-
STANDINGS OF BUSINESS CLOSED DOWN—WHETHER ALLOWABLE—
SEPARATE BUSINESS OR SAME BUSINESS—QUESTION OF FACT.

The assesseees, who were the selling agents of a textile mill at Indore, had entered into an agreement with the mill, whereby the assesseees were to be paid by the mill a commission of one per cent. on the gross sale proceeds of all the cloth of the mill and the commission was to be due to them on the 31st of December every year and was to be paid immediately thereafter. The assesseees had a shop at Bombay and another at Indore. Sales were effected in Indore, being on terms f. o. r. Indore to Bombay merchants and the purchase moneys were received in the form of hundis drawn by the assesseees through their Indore shop and accepted by the Bombay purchasers. The hundis were collected and after realisation were paid to the company in Indore by the assesseees in

Bombay and the commission was thus ultimately paid outside British India. The Income-tax authorities held that the source of the commission was the receipt of the proceeds of sale on which the commission was calculated and therefore the commission accrued or arose or was received in British India :

Held, that it was the sale and not the receipt of the sale proceeds which was the real source of the commission and, as the sale took place in Indore even though the proceeds of the sale were received in Bombay, the commission did not accrue or arise, nor was it received, in British India within the meaning of Section 4 (1).

COMMISSIONER OF INCOME-TAX *v.* SARUPCHAND [1930] (33 Bom. L.R. 382) distinguished.

Apart from the above commission agency business, the assessee carried on two other businesses, one of banking and cotton speculation and the other of cotton jatha business, in two different names. They also kept two separate books of account for these businesses. The cotton jatha business was closed before the year of assessment. The Income-tax authorities held that the two businesses were separate and therefore disallowed certain expenses incurred by the assessee in collecting the outstanding of the cotton jatha business in calculating the profits of the other business :—

Held, that the question whether these two businesses were separate businesses or were really two branches of the same business was a question of fact and in this case there was evidence on which the Income-tax authorities could come to the conclusion they had arrived at.

Cases referred to :—

Arunachalam Chetty *v.* Commissioner of Income-tax (1928) I.L.R. 52 Mad. 296.

Commissioner of Income-tax *v.* Sarupchand (1931) 55 Bom. 231 ; A.I.R. 1931 Bom. 236 ; 33 Bom. L.R. 382 ; 5 I.T.C. 108.

Scales *v.* George Thompson & Co. Ltd. (1927) 13 Tax Cas. 83 ; 138 L.T. 331.

South Indian Industrials *v.* Commissioner of Income-tax, Madras (1935) 3 I.T.R. 11 ; 8 I.T.C. 128 ; 58 Mad. 433 ; A.I.R. 1935 Mad. 330 ; 157 I.C. 143.

Case referred to the High Court by the Commissioner of Income-tax, Central (Bombay), under Section 66 (2) of the Indian Income-tax Act (XI of 1922), for the decision of the questions of law mentioned in para. 7 of the Commissioner's Statement of Case : (Income-tax Reference No. 1 of 1942).

STATEMENT OF CASE.

MY LORDS,

Under Section 66 (2) of the Indian Income-tax Act (XI of 1922) (hereinafter referred to as the Act) and at the instance of Messrs. Hiralal Kalyanmal including Messrs. Tillockchand Kalyanmal, 12-26 Bhuleshwar, Bombay (hereinafter referred to as the assessee), I have the

honour to refer to your Lordships' decision the questions of law set out in paragraph 7 below which have arisen out of the income-tax and super-tax assessments of the assesseees for the financial year 1935-36.

2. **Facts of the case.**—The assesseees carry on in Bombay the business of Banking and Speculation, and also that of Selling Agents to the Kalyanmal Mills, Ltd., Indore; and, in addition, they carry on, in Indore, the business of Secretaries, Treasurer and Managing Agents of the above-mentioned Kalyanmal Mills, Ltd. (hereinafter referred to as the Company). The terms under which the assesseees act as the Secretaries, Treasurers and Managing and Selling Agents of the Company are evidenced by an Agreement dated.....of 1919 made between the Company and the assesseees at Indore as subsequently modified by a Resolution of the Shareholders of the Company dated the 29th July 1933. Copies of the above-mentioned agreement and of the Resolution are attached hereto and collectively marked as Exhibit 'A'.

3. By clause 6 of the said Agreement, Exhibit 'A', it is provided that the Company shall defray the expenses of the assesseees' office at Indore and at Bombay, to enable the latter to transact their business of Secretaries, Treasurers and Agents of the Company, and that, in the alternative, the Company shall pay the assesseees fixed monthly allowance for the purpose. Clause 4 of the said Agreement deals with the remuneration payable to the assesseees in consideration of their services rendered as the Selling Agents of the Company. Under the said clause as modified by the said Resolution of the Shareholders of the Company dated the 29th July, 1933, the assesseees are entitled to a commission of 1% on the *gross sale proceeds* of all cloth and yarn of the Company.

4. The assesseees have a shop at Bombay, and another at Indore, for the sale of cloth and yarn produced by the Company's Mills at Indore. Both shops are maintained by the assesseees at the expense of the Company, in accordance with the terms of the said Agreement. Cloth and yarn manufactured by the Indore Mills are sold at the said two shops.

5. During the accounting period in question (the calendar year 1934), in addition to realising monies in respect of sales effected by the Bombay shop, the assesseees realised hundies in Bombay to the extent of Rs. 3,37,170 net on account of sales of cloth effected by their Indore shop to Bombay merchants. This amount was, after realisation, paid to the Company, and the necessary adjustment entry to that effect was accordingly made by the assesseees in the books of their Bombay shop. Commission at the rate of 1% was earned by the assesseees on this amount, and the Income-tax Officer, Section VII (Central), in the course of assessment in respect of the year 1935-36, treated the said commission, amounting to Rs. 3,362, as earned and received by them in

Bombay, and he, therefore, added back the commission so earned and received to the assessee's income, and assessed them to income-tax and super-tax on this amount. A copy of the Income-tax Officer's assessment order is annexed hereto marked Exhibit 'B'. The assessee contended that, as the sales were effected direct by the Indore shop, the Bombay shop had nothing to do with the earning of the commission, and therefore claimed before the Appellate Assistant Commissioner that the amount should be deleted from their assessable income. A copy of the assessee's grounds of appeal before the Appellate Assistant Commissioner is annexed hereto marked Exhibit 'C'. The Appellate Assistant Commissioner, however, held that the sale proceeds accrued in British India, and that, therefore, the commission at 1% on the sale proceeds is also taxable to British Indian income-tax and super-tax. A copy of the orders passed by the Appellate Assistant Commissioner is attached hereto marked Exhibit 'D'. The assessee thereupon approached me with a request to set aside the assessment made by the Income-tax Officer in exercise of my powers under Section 33 of the Act, or, in the alternative, to refer the questions of law that arise from the Income-tax Officer's assessment order for your Lordships' decision. Copies of their petitions to me are annexed hereto marked collectively as Exhibit 'E'. After hearing the assessee's Advocate upon the said petition, as I am not prepared to set aside the assessment in respect of Rs. 3,362 mentioned above, I submit the question of law, arising in respect of this matter, as question (1) set out in paragraph 7 below, for your Lordships' decision.

6. The assessee has also requested me to refer for your Lordships' decision the question of law arising from the Income-tax Officer's refusal to allow a sum of Rs. 5,571 as an item of deductible expenditure from the assessment in question. The assessee, in the name of Maneckchand Kalyanmal, had been doing Cotton Jatha business up to the accounting year 1921-22 (Samvat 1978-79), when they apparently discontinued it. In the course of carrying on the said business, the assessee had advanced a sum of money to one Rampratap Mahadeo which, together with brokerage and interest, amounted to Rs. 17,537 at the close of the accounting year 1921-22 (Samvat 1978-79). The said amount was not repaid and remained debited in the books of the defunct Cotton Jatha business and was at no time entered into the books of the assessee's other business (*viz.*, Banking, Speculation, etc.), which is now continuing. With a view to recovering the said amount, the assessee filed a suit on the 12th March 1930 in the Bombay High Court against the debtor. Having failed in the High Court, the assessee litigated the matter up to the Privy Council who also decided

against them. The judgment of the Privy Council was pronounced during the accounting year, and the assesseees claimed that the sum of Rs. 5,571 which they expended during that year on account of law charges for conducting their case in the Privy Council, should be allowed as a deductible item of expenditure against their assessable income from all sources for that year. The Income-tax Officer refused to do this on the ground that the debit balance which was the subject matter of the suit did not find a place in the books produced by the assesseees for their assessment in question, and that, in any case, as the loss, if any, had occurred in a business of the assesseees which had long since been closed, the expenses incurred to realise it could not be allowed as a deduction from the profits made in an entirely different business of the assesseees. An appeal against this decision of the Income-tax Officer was rejected by the Appellate Assistant Commissioner, A-Range, Bombay. The said orders of the Income-tax Officer and the Appellate Assistant Commissioner are annexed as Exhibits 'B' and 'D' respectively. The assesseees have asked me to refer to your Lordships the question of law arising from the Income-tax Officer's order in case I am unwilling to exercise my revisional powers under Section 33 in their favour. The question of law that arises in this connection is question (2) in paragraph 7 below.

7. Questions for decision.—The two questions of law that arise for your Lordships' decision are :—

“(1) Whether the commission of 1% realised by the assesseees on the value of the hundis collected by them in Bombay in respect of the cloth sold by their Indore shop to merchants in Bombay, is liable to be assessed to payment of income-tax and super-tax in British India.

(2) Whether there was material before the Income-tax Officer on which he could come to the conclusion that the Cotton Jatha business, in respect of the legal expenses for which allowance has been claimed by the assesseees, was a separate business of the assesseees which had been closed at the time of the assessment in question.”

8. Opinion of the Commissioner.—As required by Section 66 (2) of the Act, I submit for your Lordship's consideration my opinion on the two questions of law set forth above.

9. Question (1).—Section 4 (1) of the Act as it stood before amendment in 1939 applies to all income, profits or gains, as described in Section 6, from whatever source derived, accruing or arising, or received in British India, or deemed under the provisions of the Act to accrue or arise or to be received in British India. In the present case the income is the commission on the sale proceeds of the cloth sold by the assesseees' Indore shop to certain merchants in Bombay. Though the sale

contracts were concluded in Indore and the sale price was quoted as "f. o. r." Indore, it would, as decided by this Honourable Court in the similar case of *Sarupchand Hukamchand v. Commissioner of Income-tax, Bombay*¹, be material to look to the place where the sale proceeds are realised, in order to locate the material source of the income rather than to the place where the contract was concluded as the income could be said to arise or accrue in no more than perhaps a purely metaphorical sense at the place where the contract is concluded. The sale proceeds in respect of which the assessee earned the commission in question were realised in Bombay, and the assessee was, under the terms of the contract responsible for the bad debts, if any; the income on account of the commission on these sale proceeds must therefore be treated as having accrued in Bombay.

10. However, even if it were assumed that the income did not actually accrue or arise in Bombay, in my humble opinion, there is no doubt that the income was *received* in Bombay, as the assessee's accounts in Bombay contain entries relating to the receipt of the sale proceeds and the subsequent credit thereof to their Indore shop. According to Clause 18 of the Agreement with the Company, the assessee was at liberty to pay² themselves out of the monies of the Company all sums due to them for commission or otherwise. Since the sale proceeds from the merchants in Bombay were realised by the assessee in Bombay in the first instance, the assessee had the right at that point of time to appropriate therefrom the commission due not only on those sales, but on all sales effected by the Indore shop. The criterion of first receipt under Section 4 (1) as laid down in the case of *Sir Ali Imam*³ is that "the receipt of the income referred to in Section 4 must.....refer to the first occasion upon which the recipient got the money under his own control" (*vide* page 405 *ibid*). Thus, since the sale proceeds from which the assessee was at liberty to appropriate their commission, were received in Bombay, it is, in my humble opinion, correct to say that the commission itself was received there. In the case of *Sir Sarupchand Hukamchand*¹, his Lordship, the Chief Justice, observed that "the fact that the commission might have been segregated and paid in British India seems to me to have an important bearing upon the question" (*vide* page 112 *ibid*). Attention is, in this connection, also invited to the judgment of the Lahore High Court in the case of *Tora Gul Boi*³ where, upon a question as to whether the assessee was liable to be taxed on his commission on sale proceeds first received in England and then brought to British India, the decision turned upon the fact that the assessee, at the time of receipt of the sale proceeds in England, *was not*

(1) (1930) 38 Bom. L.R. 382; 5 I.T.C. 108.

(3) (1926) 2 I.T.C. 164 & 346.

(2) (1924) 1 I.T.C. 402.

entitled to appropriate any amount towards his commission because no rate of commission had been agreed upon at the time. In the case which is now before your Lordships, the assessee not only received the sale proceeds in British India, but were also entitled at the time of receipt to retain and appropriate a definite share therefrom on account of their commission.

I therefore humbly submit that your Lordships' answer to this question should be in the affirmative.

11. *Question (2).*—Whether a business is running or closed is clearly a question of fact which has to be decided by the Income-tax Officer, and, therefore, the only question of law that can arise in respect of this particular claim of the assessee is whether there was material on which the Income-tax Officer could come to the conclusion that the Cotton Jatha business had been discontinued. The principal facts on which the Income-tax Officer relied in coming to the said conclusion are:—

(i) that the accounts for the year 1921-22 are the very last accounts in which any profit or loss in connection with Cotton Jatha business is shown by the assessee;

(ii) that in the records of assessment proceedings for 1924-25 the assessee stated before the Examiner of the Income-tax Office who examined their books that their Cotton Jatha business had been closed nearly two years back. (The Examiner's report is annexed hereto as Exhibit 'F'); and

(iii) that the assessee, in their additional grounds of appeal filed before the Appellate Assistant Commissioner on 2nd April 1940, stated that the assets and liabilities of Maneekchand Kalyanmal were recovered by them *after the Jatha business was closed*.

I submit that, having regard to the facts above stated, there was evidence on which the Income-tax Officer could arrive at the conclusion he did regarding the fact of the discontinuance of the Cotton Jatha business.

12. It has been contended by the assessee that the cloth-selling agency business and the Cotton Jatha business were only two different departments of the one entire business of the assessee, and that this is borne out by the fact that the incomes from both these departments were assessed jointly in the hands of the assessee up to and for the assessment year 1923-24. This is, however, not a fact. The cloth-selling agency was owned by an unregistered firm in which the assessee had a 12 anna share and one Ahmed Rahim had a 4 anna share. The assessment of the income from the cloth-selling agency was, therefore, made in a separate case altogether, and not along with the income from the Cotton Jatha business.

13. The personal business of the assesseees as distinct from the cloth-selling agency business of the above-mentioned firm, consisted of two separate businesses, *viz.*, cotton, speculation and banking business, on the one hand, and Cotton "Jatha" business on the other. Separate sets of account books were maintained for these two businesses. The first was styled as the "Pedhi" of *Tillockchand Kalyanmal*, while the second business was conducted in the name and style of *Maneckchand Kalyanmal*. Till 1923-24 the assessment of the income from the "Pedhi" and "Cotton Jatha" businesses was made jointly in the name of the assesseees as they were the owners of both these businesses. They were, however, entirely different businesses. The cotton Jatha business consisted in selling cotton belonging to up-country clients and earning income thereby in the form of brokerage, godown rent, muccadami, insurance differences etc., while the "Pedhi" business, on the other hand, was in banking, speculation and cotton on the assesseees' own account. The Cotton Jatha business was closed in Samvat year 1978-79 (Maru Account year from the 31st October 1921 to the 20th October 1922). This was the last year in which there was any income from this business, and it was assessed in the assessment year 1923-24. After this year, the said business did not yield any income whatsoever as it was entirely closed.

14. Once it is conceded that there was such discontinuance, the assesseees' claim to recover any portion of the legal expenses incurred in connection with the recovery of the assets or outstandings of the discontinued business cannot be sustained, as such expenditure cannot be treated as one incurred solely for the purpose of earning the profits and gains which were actually assessed to income-tax in the hands of the assesseees in the year in question. This principle has been clearly laid down in *B.C.G.A. (Punjab) Ltd. v. Commissioner of Income-tax, Punjab*¹ and in *South Indian Industrials Ltd. v. Commissioner of Income-tax, Madras*².

I therefore humbly submit that your Lordships' answer to the second question should also be in the affirmative.

15. I humbly request that, in accordance with Section 66 (5) of the Act a copy of your Lordships' judgment may be forwarded to me for necessary action."

M. C. Setalvad, for the Commissioner.

Sir J. B. Kanga with *R. J. Kolah*, for the assesseees.

JUDGMENT.

BEAUMONT, C. J.—This is a reference made by the Commissioner of Income-tax under Section 66 (2) of the Income-tax Act of 1922 raising two quite separate and distinct questions.

(1) (1937) 5 I.T.R. 279.

(2) (1935) 3 I.T.R. 11.

The first question is "Whether the commission of one per cent. realised by the assesseees on the value of the hundis collected by them in Bombay in respect of the cloth sold by their Indore shop to merchants in Bombay is liable to be assessed to payment of income-tax and super-tax in British India."

The facts in relation to that question are that by an agreement made in 1919 between the Kalyanmal Mills, Ltd., which was a joint stock company registered in Indore of the one part, and the assesseees of the other part, the assesseees were to be entitled, amongst other things, to be paid the Company a commission at the rate of one per cent. on the gross sale proceeds of all cloth and yarn of the Company, and it was provided in clause (5) of the agreement that the commission should be due to the assessee firm yearly on the 31st day of December in each and every year during the continuance of the agreement and be paid immediately thereafter. The facts as found are that sales were effected in Indore, being on terms F. O. R. Indore; the purchasers being Bombay merchants, the purchase money were received in the form of hundis drawn by the assesseees through their Indore shop, and accepted by the Bombay purchasers; such hundis were collected by the assesseees in Bombay, and after realisation paid to the Company in Indore. So that, the position being that sales were effected outside British India, the proceeds of such sales were collected by the assesseees in British India and the commission of one per cent. was ultimately paid outside British India, the question is whether it can be said that the commission of one per cent. accrued or arose in British India within the meaning of Section 4 (1) of the Income-tax Act. The commission payable at the end of the year was paid in Indore and not received in British India.

We were referred to a decision of this Court in *Commissioner of Income-tax v. Sarupchand*¹, in which the facts were somewhat similar, but there were two important distinctions. In that case the assesseees were also selling agents of a mill company registered in Indore, and they had an agreement under which they were entitled to a commission of one and a half per cent. on the gross sale proceeds of all cloth produced by the mill. So that the agreements in the two cases were very similar, except that there does not appear to have been any provision in the agreement dealt with in *Commissioner of Income-tax v. Sarupchand*² that the commission was to be payable at the end of the year. In that case sales were effected in Bombay, and the moneys were received in Bombay, and the Court held that in that case, though rather near to the line, the commission accrued in British India. The court held

(1) (1930) 33 Bom. L.R. 382.

the question to be whether the real source of the commission was the agreement made in Indore or the sales in Bombay and that the sales in Bombay were the tax source. The Court relied to some extent on the fact that under the agreement the assesseees could deduct their commission from the proceeds of sales which they received in Bombay. Now, in this case the sales were not in Bombay, but in Indore, and the assesseees could not deduct their commission until the end of the year, because nothing was payable until the end of the year. Those are two important distinctions.

The argument on behalf of the Commissioner in this case is that the source of the commission is the receipt of the proceeds of sale on which the commission is calculated. But, in my opinion, that is not so. I think the source of the commission is the sale which took place in Indore. The commission would be payable although the proceeds of sale were not actually received, if the company voluntarily released purchasers from their obligation to pay. In my opinion, it is impossible to say that the commission accrued or arose at the place where, and at the time when, the purchase moneys were received. I think it is more accurate to say, as we said in *Commissioner of Income-tax v. Sarupchand*¹, that it is the sale which is the real source of the commission, and as in this case the sale took place in Indore, whereas in *Commissioner of Income-tax v. Sarupchand*¹ the sale took place in Bombay, the decisions in the two cases must necessarily be different.

I would, therefore, answer the first question in the negative.

The second question arises in this way. The assesseees had, apart from their commission agency business, two other businesses, one of them being cotton speculation and banking, and the other cotton Jatha business. The findings of the Commissioner are that these were two separate businesses; separate sets of account books were maintained for the two businesses; they were conducted in different names; and to a great extent they were distinct in their character. The cotton Jatha business consisted in selling cotton belonging to up-country clients and earning income thereby in the form of brokerage, godown rent, muccadami, insurance differences, etc.; while the other business consisted of banking, speculation and cotton on the assesseees' own account. On those facts the Commissioner came to the conclusion that the two businesses were separate. On the other hand, the assesseees maintain that they were two branches of one business. The relevance of the question is this. The cotton Jatha business was closed down before the year of assessment, but in the year of assessment the

(3) (1930) 33 Bom. L.R. 382.

assessee incurred certain expenses in endeavouring to collect outstandings of that business. If the business was still subsisting, because it was merely a branch of a still subsisting business, then the expenses would be allowable under Section 10 (2) (ix) of the Income-tax Act. If, on the other hand, the cotton Jatha business was a distinct business, and it had ceased to exist before the year of assessment, the expenses incurred in relation to it would not be allowed against the profits of the other business.

Now, whether these two businesses were separate businesses or were really two branches of the same business, is obviously a question of fact for the Commissioner to decide, and the only question raised, and the only question that can be raised, is: "Whether there was material before the Income-tax Officer on which he could come to the conclusion that the cotton Jatha business, in respect of the legal expenses for which allowance has been claimed by the assessee, was a separate business of the assessee which had been closed at the time of the assessment in question." All that we have to consider is whether there was evidence before the Commissioner on which he could reach the conclusion that these were two separate businesses. We were referred to various cases which demonstrate that it is not always easy to determine whether businesses are independent businesses, or separate branches of the same business. But the difficulty of determining a question of fact does not make it a question of law.

We were referred to *Arunachalam Chetty v. Commissioner of Income-tax*¹, which was a decision of a Full Bench of the Madras High Court, and another decision of a Full Bench of the same Court in *S. I. Industrials v. Commissioner of Income-tax, Madras*², and in those two cases the Courts to a great extent adopted different views. We were also referred to a decision of Mr. Justice Rowlatt in *Scales v. George Thompson & Co., Ltd.*³ I think it would be very difficult, if not impossible, to formulate any rules for determining questions of this nature. It is obvious that mere common ownership of the businesses does not mean that they are merely branches of the same business. It is also I think obvious that the mere fact that the two businesses are of a distinct nature does not necessarily mean that they are distinct businesses. You can have two branches of a multiple store, one selling drugs, and the other selling cloth. Nobody would suggest that these two departments constitute two different businesses. On the other hand, if you have a shop in Bombay selling cloth, and a shop in Ahmedabad selling drugs under different names and different management and under separate accounts, common ownership would hardly

(1) (1928) I.L.R. 52 Mad, 296. (2) (1935) 3 I.T.R. 11. (3) (1927) 13 Tax Cas 83,

make them one business. Mr. Justice Rowlatt in *Scales v. George Thompson & Co., Ltd.*¹, suggests that there must be some sort of inter-relation between the two businesses, to constitute the branches of the same business. At any rate all these cases recognise the fact that this matter is a question of fact to be determined by the Commissioner, and if there is any evidence enabling him to determine the question, then his determination is final. I am unable to say that there was no evidence in this case on which the Commissioner could come to the conclusion which he reached, that these were two distinct businesses. The two businesses may have overlapped to some extent, but there was evidence that they were separate in their character. I am not prepared to say that there was no evidence on which the Commissioner could reach the conclusion he reached.

Therefore, the answer to the second question will be in the affirmative.

There will be no order as to costs, each side having succeeded on one question.

KANIA, J.—The Commissioner has referred two questions for the opinion of the Court. On the first question the relevant facts are that the assesseees are the managing agents and also the selling agents of a textile mill at Indore. An agreement in that connection was made between the Mill Company and the assesseees in 1919. That agreement provides for the opening of shops at Indore and Bombay for the business of the Company, and the Company has agreed to pay the costs of running those two shops. At both those shops cloth and yarn produced by the Mill Company were sold. In respect of the sales effected in Bombay by the assesseees they earned the selling agency commission for which they have been assessed, and the same is paid. In respect of the sales effected at the Indore shop the facts are founded in the statement of the case submitted by the Commissioner. According to that statement sales took place at the Indore shop on F. O. R. terms to Bombay merchants. To recover the sale proceeds the Indore shop drew hundies on the Bombay merchants, which were in due course accepted and honoured by the Bombay merchants. The proceeds of those hundies were received by the assesseees in Bombay. On those facts it is argued on behalf of the Commissioner that the commission at one per cent. on those gross sale proceeds either accrued or arose in British India, or was received in British India. *Commissioner of Income-tax v. Sarupchand*² was relied upon in this connection. The facts as reported in that case clearly show that the sales were effected

there by the assesseees in Bombay to Bombay merchants, and the sale proceeds were all recovered in Bombay. Therefore, not only the contract of sale but the sale took place in Bombay in that case. On those facts the Court found that the income accrued in British India. In the present case those two vital factors are wanting. The sale took place at Indore, and the property in the goods also passed to the Bombay merchants as soon as the goods were railed at Indore. Therefore, the sale was completed at Indore.

It was argued on behalf of the Commissioner that the receipt of the sale proceeds is the source from which the income accrued. In my opinion, this contention is unsound. The receipt of the sale proceeds at a particular place is not stated to be a part of the contract between the Mill Company and the merchants. The accident, therefore, of the sale proceeds being received in Bombay cannot make the source of the income in Bombay. To illustrate, suppose instead of the assesseees receiving the sale proceeds, the same were recovered by a bank in Bombay, and credited by the Bank to the account of the assesseees which was being operated upon by the assesseees from Indore and also by their manager in Bombay, I fail to see how the receipt of the sale proceeds from the merchants in Bombay by the bank would constitute a source of the income in Bombay. The underlying assumption that the receipt of the sale proceeds is a source, in my opinion, is unjustified. The commission had to be calculated on the amount of the sale proceeds. It was payable however only after the end of the year. Therefore, the receipt of the sale proceeds does not give rise to the accrual of the income in British India.

The second part of the argument was that the receipt of the sale proceeds included the receipt of the commission in British India, and, therefore, the commission was received in British India. This contention is also unsound. The amount that was received was only the sale proceeds. That amount, when paid to the Mill Company, would give rise to a right in the selling agents to receive their commission. To put it in other words, supposing the selling agent failed to pay the amount to the Mill Company, would they have a right to receive any commission at all? It seems to me certainly not, because they have committed a breach of their agency agreement, and, therefore, they will not be entitled to any remuneration for their work as agents. The receipt of the sale proceeds, therefore, means only the sale price received on behalf of the Company, and because the agents are entitled to a commission worked out on the amount of the sale proceeds, the receipt of the sale proceeds does not amount, in my opinion, to the receipt of the selling agency commission.

The second question is limited by its very nature. The Court has jurisdiction only to inquire whether there was any evidence before the Commissioner for his conclusion on a question of fact that the two businesses were separate. According to the facts stated in the reference, the two businesses were one of banking and speculation which, I understand, would mean buying and selling cotton for forward delivery, and the other of commission agency which includes the receipt of cotton from up-country constituents, advancing money to the constituents and the earning of interest, brokerage, muccadami, insurance differences, etc., as stated in the reference. They were done in two different names. The assessee had kept also two separate books of account, and they certainly closed the commission agency business many years ago. On those facts the Commissioner had come to the conclusion that the two businesses were separate, and I do not think that the conclusion of the Commissioner is liable to be disturbed by this Court on the ground that he had no evidence before him to show that. The question of fact is bound to vary in each case, and little assistance is likely to be derived from reported decisions which held that in particular cases the businesses were separate or were the same. It is difficult, if not impossible, to lay down any general standard by which the distinction could be clearly made, and decided. The reported cases show that ownership is not the sole criterion. In the same way the decisions also show that the nature of the businesses must in some way be shown to be connected; otherwise there would be some reason to believe that the businesses were separate. In the present case the assessee has kept the two businesses in separate names, and it cannot be disputed that an individual may carry on a commission agency business in cotton, without necessarily doing the business of a merchant, and vice versa. The fact that one business is done, while the other is closed, shows that the two are capable of being conducted independently. Under the circumstances, I am not prepared to say that the Commissioner had no evidence to come to the conclusion he did on this question of fact.

I agree, therefore, that the answers should be as indicated in the judgment of the learned Chief Justice, and I agree to the order made.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME-TAX v. SIR HOMI M. MEHTA.

BEAUMONT, C. J., and KANIA, J.

April 7, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE AMENDMENT OF 1939), SECS. 4, 7, 10 (2) (ix), 12—BUSINESS EXPENDITURE—GIFT OF SUM TO COMPANY IN FINANCIAL DIFFICULTIES BY MANAGING DIRECTOR, PROMOTER AND PRINCIPAL SHAREHOLDER TO SAVE HIS CAPITAL, SALARY AND BUSINESS REPUTATION—WHETHER ALLOWABLE DEDUCTION—PROFITS FROM SALE OF SHARES—WHETHER INCOME OR CAPITAL.

The assessee who was the promoter, managing director and principal shareholder of a company made a gift of Rs. 3 lacs to the company when it was in financial difficulties and claimed this sum as a deduction from his assessable income on the ground that if he had not made the gift the company would have failed and he would have lost his capital invested in the company, his salary, and his business reputation and credit :

Held, that the sum of Rs. 3 lacs paid by the assessee to the company was not expenditure allowable under Section 10 (2) (ix) or under the provisions of Section 7 or Section 12 of the Act.

BEAUMONT, C. J.—*The maintenance of business reputation is undoubtedly a capital asset.*

SOUTHERN (H. M. INSPECTOR OF TAXES) v. BORAX CONSOLIDATED LTD. [1942]) 10 I.T.R. Suppl. 1) *distinguished.*

Held also, on the facts, counsel for the assessee agreeing, that there was evidence before the Income-tax authorities on which they could come to the conclusion that the sum of Rs. 96,537 which had been included in the assessee's income represented profits from trading in shares and not capital appreciation.

Case referred to :—

Southern (H. M. Inspector of Taxes) v. Borax Consolidated Ltd. (1942) 10 I.T.R. Suppl. 1; (1940) 4 A.E.R. 412; (1941) 1 K.B. 111; 85 S.J. 94.

Case referred to the High Court of Bombay by the Commissioner of Income-tax, Bombay, under Section 66 (2) of the Indian Income-tax Act (XI of 1922), for the decision of the questions of law mentioned in para. 5 of the Commissioner's Statement of the Case: (Income-tax Reference No. 5 of 1941).

STATEMENT OF CASE.

“MY LORDS,

Under Section 66 (2) of the Indian Income-tax Act (XI of 1922) (hereinafter referred to as “the Act”) and at the instance of Sir Homi M. Mehta of Bombay (hereinafter referred to as “the assessee”), I have

the honour to refer for your Lordships' decision the questions of law set out in paragraph 5 below, which have arisen out of the assessment of the assessee for the financial year 1937-38, the relevant accounting period being the calendar year 1936.

2. Facts of the case.—The assessee is a resident of Bombay and his sources of income are (1) Dealing in shares, (2) Dividends, (3) Salary, (4) Interest on securities, (5) Interest on fixed deposits, and (6) Shares in various partnerships. He was assessed to income-tax and super-tax for the assessment year 1937-38 by the Income-tax Officer, A Ward, Bombay, on a total income of Rs. 5,22,400. A copy of the assessment order is annexed and marked A. In computing this income, the Income-tax Officer included a sum of Rs. 96,537 being the profit on the sale of shares worth Rs. 8,27,694, and he disallowed a payment of Rs. 3,28,645 made by the assessee on behalf of the British India General Insurance Company of which he was the promoter and is at present the Chairman and Managing Director and in which he owns a large number of shares. The assessee claimed (i) that the sum of Rs. 96,537 was capital appreciation and as such should not be included in his taxable income, and (ii) that the sum of Rs. 3,28,645 was expenditure incurred by him for the purpose of earning income from the British India General Insurance Company and was therefore an admissible deduction.

3. Being dissatisfied with the Income-tax Officer's order the assessee filed an appeal to the Appellate Assistant Commissioner, A Range, Bombay, under Section 30 of the Act. The Appellate Assistant Commissioner did not accept his contentions and upheld the decision reached by the Income-tax Officer. A copy of the appellate order is annexed and marked B.

4. The assessee then made an application to the Commissioner of Income-tax, Bombay, in which he requested that the assessment made by the Income-tax Officer be revised under Section 33 of the Act, or in the alternative that a reference be made to the High Court under Section 66 (2). A copy of the application is annexed and marked C.

5. Questions for decision.—In his application the assessee raised six alleged questions of law of which the first two relate to the item of Rs. 96,537 and the other four to the item of Rs. 3,28,645. I think all the points at issue are covered by the following two questions which I accordingly refer for your Lordships' decision :—

(1) Whether in the circumstances of the case there was evidence before the Income-tax authorities on which they could come to the conclusion that the sum of Rs. 96,537, which has been included in the assessment, represented profits from trading in shares and not capital appreciation; and

(2) Whether in the circumstances of the case the sum of Rs. 3,28,645 paid by the assessee on behalf of the British India General Insurance Company is expenditure allowable under Section 10 (2) (ix) or under the provisions of Section 7 or Section 12 of the Act.

6. **Opinion of the Commissioner.**—It is admitted that the assessee does business in shares. His contention is that only his dealings in Vaida (forward) shares were business and that his dealings in ready shares were all for investment purposes and were not incidental to any business. The profits from dealings in Vaida shares are not in dispute but it may be noted that the figures given in the appellate order in fact relate to the following assessment year. The net profit earned in Vaida business during the year now under consideration was Rs. 2,01,397.

7. The profit of Rs. 96,537 which is the subject of the first question was earned through the sale of nine lots of ready shares, and the greater part of it was derived from two transactions in Tata Iron & Steel ordinary shares. The assessee purchased 2,000 such shares in October 1935 and sold them three months later in January 1936 at a profit of Rs. 38,000. He again purchased 1,300 Tata Iron & Steel ordinary shares in April 1936 and sold them in July 1936 at a profit of Rs. 33,800. These short term purchases and sales indicate an underlying intention to make a profit and not to hold the shares as investments, especially as the first lot of shares was purchased after prices had started to rise in 1935. It is sometimes difficult to say at which point investment ends and trading begins but in regard to these two transactions I do not think there can be any doubt that the purchases were made with a view to resale at a profit if the market moved favourably.

8. The balance of the assessed profit of Rs. 96,537 was derived from sales in 1936 of shares bought in 1935. The Income-tax Officer decided to treat the sales made in 1936 of shares bought in 1935 or 1936 as transactions of business in ready shares as opposed to purchases for investment. This appears to be as reasonable and fair a basis as can be arrived at in the circumstances of the case. It has to be noted that the assessee has been allowed losses in the two transactions of this type in which they occurred.

9. It is a common practice for speculators to keep some ready shares available in order to facilitate their forward purchases and sales. In the present case the assessee admittedly had a business of buying and selling shares and I think it was rightly inferred that the ready shares held by him for short periods were held as a part of that business. I submit that the mere fact of making delivery is not sufficient to

convert a business transaction into an investment. The criterion which must be applied in such cases is whether the purchases were made with a view to resale at a profit and in the present case there is in my opinion material to justify the conclusion that the purchases were made with this intention.

10. It was further claimed on behalf of the assessee, without prejudice to his main contention, that as a sum of Rs. 4,76,022 out of the sale proceeds of Rs. 8,27,694 (which was the amount realised by the sale of the shares in question) was utilised to pay off the assessee's overdraft with the Bank of India Ltd., it could not be said that all the sales of the ready shares were effected for the purpose of doing business in shares. It was claimed that as about sixty per cent. of the sale proceeds were utilised to pay off the overdraft, a sum representing about sixty per cent. of the profit of Rs. 96,537 should not in any event be treated as profit. I submit that the manner in which the sale proceeds were utilised in no way affects the question for determination or the taxability of the profit which has arisen. The existence of the overdraft is on the contrary an argument in favour of holding that the dealings in these shares formed part of the profit making scheme. The assessee has been allowed a deduction in respect of the interest paid by him on the overdraft account.

11. For the above reasons I submit that question (1) should be answered in the affirmative.

12. As regards question (2) an ex-gratia payment of £ 24,687-10-0 (equivalent to Rs. 3,28,645) was made by the assessee to "The Re-Insurance Corporation Ltd." on behalf of the British India General Insurance Company of which he was the Chairman and a principal shareholder and is at present the Managing Director. The British India General Insurance Company is a public limited company and the assessee derives income from it in the form of (1) Director's fees, (2) Managing Director's salary, and (3) Dividends on 25,000 shares which he holds out of a total of 1,00,000 shares. This company was in financial difficulties owing to a large claim made against it by a foreign company. The assessee claims that if he had not made the above gift the Company would have failed and he would have lost (i) his capital invested in the Company, (ii) his salary of Rs. 1,000 per mensem as Managing Director, and (iii) his business reputation and credit. He was satisfied that if he made the gift the Company would survive and would soon be able to pay dividends again and that his capital and dividend income and his monthly salary of Rs. 1,000 would thus be saved. Hence he claims that the amount paid by him is admissible as business expenditure under Section 10 (2) (ix).

13. I submit that the payment should be regarded as a payment to safeguard a capital asset and not as a payment made for the purpose of earning profits or gains. From the facts stated it seems reasonable to infer that the main considerations which led the assessee to make the payment were the safeguarding of his capital of 2½ lakhs invested in the Company's shares and the saving of his general business credit and reputation. These are obviously assets of an enduring character, and as was observed by Viscount Cave in *Atherton v. British Insulated & Helsby Cables Ltd.*¹, "When an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."

14. I would further submit that the business of the British India General Insurance Company, Ltd., cannot be deemed to be the business of the assessee and that the benefits which he receives from this Company are not the profits or gains of a business carried on by him within the meaning of Section 10 of the Act. For this reason also the payment is not in my opinion admissible as a deduction under Section 10 (2) (ix) as it stood before the passing of the Income-tax (Amendment) Act, VII of 1939. Nor is it admissible under any other section of the Act. The Director's fees and dividends are assessable under Section 12 and that section contains a provision corresponding to Section 10 (2) (ix) but as I have already stated I do not think it is possible to hold that the payment was made for the purpose of earning the income from these sources. As regards the income from salary the question does not arise since Section 7, as it stood before the passing of Act VII of 1939, contained no provision for a deduction of this kind.

15. For the above reasons I am of opinion that the answer to question (2) should be in the negative."

Advocate-General with G. N. Joshi, for the Commissioner.

Sir Jamshedji Kanga with R. J. Kolah, for the assessee.

JUDGMENT.

BEAUMONT, C. J.—This is a reference made by the Income-tax Commissioner under Section 66 (2) of the Income-tax Act. The year of assessment is the financial year 1937-38, and the accounting period is the calendar year 1936; so that we have to deal with the Income-tax Act of 1922 before the amendment of 1939.

(1) (1925) 10 Tax Cas. 155, at p. 192.

The Commissioner has raised two questions. The first one is :

“Whether in the circumstances of the case there was evidence before the Income-tax authorities on which they could come to the conclusion that the sum of Rs. 96,587, which has been included in the assessment, represented profits from trading in shares and not capital appreciation.”

On that question no argument has been addressed to us, and Sir Jamshedji Kanga for the assessee says that he does not wish to press the question, and agrees that it should be answered in the affirmative, that being the sense in which the Commissioner has answered it. So that we are only concerned with the second question, which is in these terms :

“Whether in the circumstances of the case the sum of Rs. 3,28,645 paid by the assessee on behalf of the British India General Insurance Company is expenditure allowable under Section 10 (2) (ix) or under the provisions of Section 7 or Section 12 of the Act.”

It appears from the case that the Insurance Company in question, which is in fact a Limited Company, though it is not so stated in the question, was promoted by the assessee, and the assessee continues to be a Director and Managing Director of the Company, for which he receives a salary, and he holds 25,000 shares out of a total of a lac of shares. The Company got into financial difficulties owing to a large claim made against it by a foreign Company, and the assessee came to the rescue of this Company, and during the accounting period made to it a gift of the sum mentioned in the question, and we have to determine whether that sum can be allowed as a deduction. It is, of course, obvious that primarily the business for the preservation of which the payment was made, was the business of the Company, and not the business of the assessee. But it is said that the payment was made, in part, in order to preserve the fees payable to the assessee as Director and Managing Director and the dividends on his shares in the Company. So far as those items of income are concerned, it seems to me that they clearly would not come within Section 10 of the Act, which deals with deductions allowable from income derived from business, but would have to be brought within the provisions of Section 12, which deals with tax on other sources of income. It is said, however, that the case may be brought within Section 10, because part of the business of the assessee consists in the promotion and financing of Companies, and that the object of this payment was to preserve such business and the assessee's reputation as a businessman, so as to secure income from future promotion of Companies.

Dealing with the particular items of income derived by the assessee from this Company, which as I have said, fall within Section 12 as income derived from other sources, a deduction can be made under Section 12 (2) for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains. It seems to me quite impossible to say that this payment was made to the Company solely for the purpose of enabling the assessee to maintain his income derived from the Director's and Managing Director's fees and dividends on shares. The object of the expenditure must have been also to preserve the value of the other 75 per cent. of the shares in the Company which the assessee did not hold. If his sole purpose had been to preserve his income derived from that particular Company, obviously a more business-like arrangement would have been to make to the Company a loan, which could have been repaid to the assessee as a debt. But the main object was to keep the Company going, to maintain his own reputation as the man who had promoted the Company.

When one comes to the expenditure under Section 10, an allowance may be made under sub-section (2) (ix) for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains. The "profits or gains" referred to must be, for the purpose of this case, the profits or gains which the assessee makes by his business of promoting Companies, and I think it impossible to say that this payment was made solely for the purpose of earning such profits or gains. It was partly for the purpose of earning the other income which falls within Section 12, partly for the protection of the income of the other shareholders in the Company, and partly for the protection of the assessee's business reputation. On this aspect of the matter, I agree with the Commissioner of Income-tax in thinking that this is a capital expenditure. The maintenance of business reputation is undoubtedly a capital asset.

Sir Jamshedji Kanga has relied on a recent decision in *Southern (H. M. Inspector of Taxes) v. Borax Consolidated, Ltd.* reported in the Supplement to the *Income-tax Reports*, Vol. X, (1942) p. 1 in which case Mr. Justice Lawrence held that where a sum of money was laid out for the acquisition or the improvement of a fixed capital asset, it was attributable to capital, but if no alteration was made in the fixed capital asset by the payment, then it was properly attributable to the revenue, being in substance a matter of maintenance, the maintenance of the capital structure or the capital assets of the Company. The Court was dealing there with an expenditure made in maintaining the title of the Company to certain land, which had been challenged in a

Court of law, and it was held that the capital asset, namely the land, remained exactly the same after maintaining the title as before. But I find it very difficult to apply that principle to so intangible a capital asset as business reputation. It is impossible to say that the assessee's business reputation remained exactly the same after the payment as before it. The object of the payment, I think, was to enhance the reputation of the assessee, and to avoid his being associated with a company which had failed. In my view, it is impossible to say that payment for the maintenance of business reputation is not payment for a capital purpose.

The answer to the second question referred to us must be in the negative.

The assessee to pay costs.

KANIA, J.—I agree. The deduction is sought to be allowed under three sections which are mentioned in question (2). Section 7 is clearly inapplicable, and the argument advanced on behalf of the assessee is, therefore, limited to Sections 10 (2) (ix) and 12 of the Act. The relevant sections to be considered are before the Amending Act of 1939.

As the payment was not made for the purpose of saving the business of the assessee, but was made to save the business of the Insurance Company, I do not think the case falls at all under Section 10 (2) (ix). Under Section 12 the decision of Mr. Justice Lawrence in *Southern (H. M. Inspector of Taxes) v. Borax Consolidated, Ltd.*¹, might have been helpful, if the facts were that the payment was made only to save certain property of the assessee. In the statement of case it is clearly stated that the assessee claimed that if he had not made the above gift, the Company would have failed, and he would have lost (1) his capital invested in the Company, (2) his salary of Rs. 1,000 per mensem as Managing Director, and (3) his business reputation and credit. It may be open to argument that the first two, namely, saving the capital invested in the Company and saving the salary, might be covered by the judgment of Mr. Justice Lawrence. But it is clear that business reputation and credit cannot be merely in relation to the Insurance Company. It must be in respect of the general business reputation and credit of the assessee as a promoter of different companies, of which he is either the Managing Director or a partner in the managing agency firm. In that view it is clear that the allowance is not *solely* for the purpose of making or earning the income, profits or gains shown under the first two items. It is in the nature of a general capital expenditure, not merely limited to this particular Insurance Company.

(1) (1942) 10 I.T.R. Suppl. 1.

I, therefore, think that the case is not clearly covered by Section 12 (2). It is claimed as an allowance, and, therefore, it is the duty of the assessee to show that it is covered by the exception. As that is not shown, the answer must be that this payment cannot be allowed as an expenditure.

Reference answered accordingly.

[IN THE PATNA HIGH COURT.]
KAMESHWAR SINGH BAHADUR

v.

GOVERNMENT OF BIHAR.

HARRIES, C.J., FAZL ALI and MANOHAR LALL, JJ.

April 1, 1942.

BIHAR AGRICULTURAL INCOME-TAX—DEDUCTIONS—CHARGES FOR COLLECTING RENT—"RENT WHICH ACCRUED DUE IN PREVIOUS YEAR"—WHETHER REFERS TO CURRENT AS WELL AS ARREAR RENT—RENT—MEANING OF—BIHAR AGRICULTURAL INCOME-TAX ACT (VII OF 1938), Sec. 6 (c).

The words "rent which accrued due in the previous year" in Section 6 (c) of the Bihar Agricultural Income-tax Act mean rent which actually fell due and first became recoverable in that year. Consequently the deduction to be allowed under Section 6 (c) of the Act in respect of collection charges is to be calculated on the total amount of rent falling due in the course of the previous year only, and not on the total rent falling due in that year together with arrears of rent realisable in respect of earlier years.

The word "rent" in Section 6 (c) does not include interest on arrears of rent. The word means what was actually agreed to be paid for the land between the landlord and the tenant.

MAHARAJA BAHADUR RAM RAN VIJAY PRASAD SINGH v. PROVINCE OF BIHAR [1942] (10 I.T.R. 446) followed.

Cases referred to :—

Maharaja Bahadur Ram Ran Vijay Prasad Singh v. Province of Bihar (1942) 10 I.T.R. 446; A.I.R. 1942 Pat. 435; 202 I.C. 128.

Slack v. Sharp (1838) 8 Ad. & E. 366; 1 New. & P. 390; 7 L.J.K.B. 225; 2 Jur. 839.

Case referred to the High Court of Judicature at Patna, by the Board of Agricultural Income-tax, Bihar, under Section 25 (3) of the Bihar Agricultural Income-tax Act (VII of 1938), for the decision of the following question of law, *viz.*, "Whether the deduction to be allowed under Section 6 (c) of the Bihar Agricultural Income-tax Act, 1938, is to be calculated in the present case on the total amount of rent falling

due in the course of the previous year only, or on the total rent falling due for that year together with arrears of rent realisable in respect of earlier years."

Miscellaneous Judicial Case No. 57 of 1941.

The facts of the case appear fully in the judgment of Harries, C.J.

P. R. Das, Murari Prasad, S. Srivatsava and G. D. Misra, for the petitioner.

Advocate-General, for the opposite party.

JUDGMENT.

HARRIES, C. J.—This is a reference made by the Board of Agricultural Income-tax, Bihar, under Section 25 (3), Bihar Agricultural Income-tax Act, in which the opinion of the Court is required upon the following question :—

"Whether the deduction to be allowed under Section 6 (c), Bihar Agricultural Income-tax Act, 1938, is to be calculated in the present case on the total amount of rent falling due in the course of the previous year only, or on the total rent falling due for that year together with arrears of rent realisable in respect of earlier years."

For the year of assessment of 1939-40 the Maharajadhiraj of Darbhanga claimed that a sum of Rs. 18,44,676-10-0 should be deducted from his agricultural income in respect of collection charges. The taxing authorities allowed a deduction of Rs. 6,80,057-15-1 and disallowed the remainder. From the order of the Income-tax Officer the assessee appealed but obtained no relief. He eventually asked the Board of Agricultural Income-tax, Bihar, to state a case, but the Board refused to do so. On application to this Court this Court by its order dated 25th August 1941, directed the Board to state a case on the question which I have already set out. Permissible deductions from agricultural income are dealt with in Sections 6 and 7, Bihar Agricultural Income-tax Act, and the relevant provision in this case is Section 6 and clause (c) thereof. Section 6 provides that

"the agricultural income mentioned in sub-clause (1) of clause (a) of Section 2 shall be deemed to be the sum realised in the previous year on account of agricultural income mentioned in the said sub-clause (1), after making the following deductions : (c) a sum equal to 12½ per cent. of the total amount of the rent which accrued due in the previous year, in respect of the charges for collecting the same."

Sub-clause (1) of clause (a) of Section 2 deals with rent or income derived from land which is used for agricultural purposes, and clause (a) of Section 6 allows a deduction in respect of collection charges of a sum equal to 12½ per cent. of the total amount of the rent which

I, therefore, think that the case is not clearly covered by Section 12 (2). It is claimed as an allowance, and, therefore, it is the duty of the assessee to show that it is covered by the exception. As that is not shown, the answer must be that this payment cannot be allowed as an expenditure.

Reference answered accordingly.

[IN THE PATNA HIGH COURT.]

KAMESHWAR SINGH BAHADUR

v.

GOVERNMENT OF BIHAR.

HARRIES, C.J., FAZL ALI and MANOHAR LALL, JJ.

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The word "rent" in Section 6 (c) does not include interest on arrears of rent. The word means what was actually agreed to be paid for the land between the landlord and the tenant.

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due in the course of the previous year only, or on the total rent falling due for that year together with arrears of rent realisable in respect of earlier years."

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Advocate-General, for the opposite party.

JUDGMENT.

HARRIES, C. J.—This is a reference made by the Board of Agricultural Income-tax, Bihar, under Section 25 (3), Bihar Agricultural Income-tax Act, in which the opinion of the Court is required upon the following question :—

"Whether the deduction to be allowed under Section 6 (c), Bihar Agricultural Income-tax Act, 1938, is to be calculated in the present case on the total amount of rent falling due in the course of the previous year only, or on the total rent falling due for that year together with arrears of rent realisable in respect of earlier years."

For the year of assessment of 1939-40 the Maharajadhiraj of Darbhanga claimed that a sum of Rs. 18,44,676-10-0 should be deducted from his agricultural income in respect of collection charges. The taxing authorities allowed a deduction of Rs. 6,80,057-15-1 and disallowed the remainder. From the order of the Income-tax Officer the assessee appealed but obtained no relief. He eventually asked the Board of Agricultural Income-tax, Bihar, to state a case, but the Board refused to do so. On application to this Court this Court by its order dated 25th August 1941, directed the Board to state a case on the question which I have already set out. Permissible deductions from agricultural income are dealt with in Sections 6 and 7, Bihar Agricultural Income-tax Act, and the relevant provision in this case is Section 6 and clause (c) thereof. Section 6 provides that

"the agricultural income mentioned in sub-clause (1) of clause (a) of Section 2 shall be deemed to be the sum realised in the previous year on account of agricultural income mentioned in the said sub-clause (1), after making the following deductions : (c) a sum equal to $12\frac{1}{2}$ per cent. of the total amount of the rent which accrued due in the previous year, in respect of the charges for collecting the same."

Sub-clause (1) of clause (a) of Section 2 deals with rent or income derived from land which is used for agricultural purposes, and clause (a) of Section 6 allows a deduction in respect of collection charges of a sum equal to $12\frac{1}{2}$ per cent. of the total amount of the rent which

accrued due in the previous year. In Miscellaneous Judicial No. 99 of 1940¹ in which a judgment was given to-day, this Court has held that the word "rent" in Section 6, clause (c), does not include interest on arrears of rent. The word means what was actually agreed to be paid for the land between the landlord and the tenant.

The contention of the assessee in this case was that the phrase "the total amount of the rent which accrued due in the previous year" meant not the actual rent that fell due in the previous year but the actual amount of rent which was realisable in the previous year. In other words, the total amount of the rent which accrued due in the previous year meant not only the actual rent which fell due in that year but rent which had fallen due in previous years and which had not been realised but could be realised in the year in question. The Income-tax authorities, however, held that the phrase "the total amount of the rent which accrued due in the previous year" meant only the actual rent which fell due in that year—in other words, the jamabandi rent for that year. The question which has to be decided is what is meant by the words "which accrued due in the previous year." If the words "rent which accrued due in the previous year" mean rent which fell due in the previous year, then the Income-tax authorities are right. On behalf of the assessee, however, it has been contended that the word "accrue" connotes growth, and, therefore, "rent which accrued due in the previous year" must mean all rent which was then recoverable, though part of it had actually fallen due in earlier years. In the Shorter Oxford English Dictionary the meaning of the word "accrue" is given as: "Fall as a natural growth or increment; to come as an accession or advantage; to arise or spring as a natural growth or result; to grow."

It must be remembered, however, that the word is used in the past tense in Section 6 (c). The actual words are: "a sum equal to 12½ per cent. of the total amount of the rent which accrued due in the previous year"; that is, 12½ per cent. of the rent which has grown due or which has actually become due in the previous year.

Reliance was placed on certain income-tax cases in which the words "accrues" or "arises" have been considered; but those cases are not applicable because the phrase in Section 6 (c) is in the past tense. What is allowed in respect of collection charges is 12½ per cent. of a sum which actually became due in the previous year. It is therefore necessary to consider when rent actually accrues or becomes due. At Common law in England rent accrued due when it became payable and at no other time. This is clearly laid down in *Slack v. Sharp*². At page 873 Patterson, J., observed:

(1) *Ram Ran Vijay Prasad Singh v. Province of Bihar* (1942) 10 I.T.R. 446.

“The question is merely when the rent accrued. Rent accrues when it becomes due, and at no other time. If there be no demise, and an action be brought merely for use and occupation, then the compensation due for such actual occupation accrues, like interest, *de die in diem*. But where there is an actual demise, and an express reservation, the rent accrues on the day named in the reservation, and on no other.”

In this province rent only accrues on the day on which it becomes payable. Section 53, Bihar Tenancy Act, is in these terms :

“Subject to agreement or established usage, a money-rent payable by a tenant shall be paid in four equal instalments, falling due on the last day of each quarter of the agricultural year.”

The rent therefore accrues due on those dates. There is a similar provision in the Chota Nagpur Tenancy Act. Section 52 of that Act provides :

“Subject to any registered agreement or local custom or usage to the contrary, a money-rent payable by a tenant shall be payable in four equal instalments falling due on the last day of each quarter of the agricultural year.”

In my view, the only rent which can be said to have accrued due in the previous year is the rent which actually fell due in that year. In that year other rent might be recoverable, such as rent which fell due in previous years and which had not been realized. It would however be straining the language of Section 6 (c) to hold that rent which had fallen due in earlier years but was recoverable in the previous year was rent which had accrued due in the previous year. The words “which accrued due in the previous year” can, in my judgment, only mean rent which fell due or became payable in that year.

It is to be observed that if the assessee's contention be well founded he might obtain a deduction for a number of years on the same rent. Assume x rupees had fallen due as rent in the previous year and y rupees was due in respect of earlier years but which remained unrealized. According to the assessee, he would be entitled to $12\frac{1}{2}$ per cent. of x plus y . In the following year let us assume x rupees again became due as rent. If none of the arrears had been realised, the assessee, according to his argument, would for that year be entitled to a deduction not only of $12\frac{1}{2}$ per cent. of x rupees but also of $12\frac{1}{2}$ per cent. on the unrealized arrears of x plus y ; that is, a deduction of $12\frac{1}{2}$ per cent. of $2x$ plus y . In such a case he would be receiving a deduction in respect of xy rupees twice over. In my view, such could never have been the intention of the Legislature.

The scheme of the section appears to me to be clear. The Legislature have adopted a rough and ready method of arriving at a

deduction to be made in respect of collection charges. The deduction is not based on actual rent realized in a particular year but on the rent which fell due in that year, and it matters not whether such rent has or has not been collected. Each year the assessee is given $12\frac{1}{2}$ per cent. on the jamabandi rent, and that may in some years be a generous deduction, whereas in others it may not be so generous. Where arrears of previous years have been collected, the deduction is not generous, but where there are no arrears and the rent which fell due in the previous year has not been collected in its entirety, the deduction is really a generous one. It is a rough and ready method of arriving at a fair deduction for collection charges, and in my judgment the view of the Income-tax authorities must be maintained. "Rent which accrued due in the previous year" can only mean rent which actually fell due and first became recoverable in that year.

For the reasons which I have given, I would therefore answer the question submitted as follows: The deduction to be allowed under Section 6 (c), Bihar Agricultural Income-tax Act, 1938, is to be calculated in the present case on the total amount of rent falling due in the course of the previous year only, and not on the total rent falling due in that year together with arrears of rent realizable in respect of earlier years. The assessee must pay the costs of this proceeding, and I would assess the hearing fee at Rs. 100.

FAZL ALI, J.—I agree.

MANOHAR LALL, J.—I agree.

Reference answered accordingly.

[IN THE NAGPUR HIGH COURT.]

Mst. PANNABAI

v.

COMMISSIONER OF INCOME-TAX, C. P. & U. P.

NIYOGI and DIGBY, JJ.

December 18, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 3, 55—HINDU UNDIVIDED FAMILY—WIDOW OF LAST SURVIVING COPARCENER AND WIDOW OF LAST SURVIVING COPARCENER'S FATHER—WHETHER CONSTITUTE A HINDU UNDIVIDED FAMILY—WHETHER INCOME RECEIVED ASSESSABLE AS INCOME OF THE FAMILY.*

* The Hindu Women's Rights to Property Act, 1937, had no application here, as both the husband of the assessee and the assessee's father-in-law died before the commencement of the Act.—ED.

The widow of the last surviving coparcener of a Hindu undivided family adopted a son after her husband's death. The son also died issueless leaving behind him his wife (the assessee) and her mother-in-law. The question being whether the assessee and her mother-in-law who was entitled to maintenance constituted a Hindu undivided family within the meaning of Section 55 and whether the income received by the assessee should be assessed as the income of the Hindu undivided family :

Held, that the assessee and her mother-in-law did not constitute a Hindu undivided family within the meaning of that term as used in Section 55. The assessee was the sole owner of the property which had devolved on her on the death of her husband and the income from the property was liable to be assessed as the income of an individual and not as the income of the Hindu undivided family notwithstanding that it was subject to the right of maintenance of her mother-in-law.

Cases referred to :

Baji Rao v. Ramkrishna (1941) I.L.R. 1941 Nag. 707.

Bijoy Gopal Mukherji v. Krishna Mahishi Debi (1907) 34 Cal. 329; 34 I.A. 87; 9 Bom. L.R. 602; 11 C.W.N. 424; 5 C.L.J. 334; 2 M.L.T. 133; 17 M.L.J. 154; 4 A.L.J. 329.

Commissioner of Income-tax, Bombay v. Laxminarayan (1935) I.L.R. 59 Bom. 618; 3 I.T.R. 367; 8 I.T.C. 239; A.I.R. 1935 Bom. 412; 37 Bom. L.R. 69.

Kalyanji Vithaldas v. Commissioner of Income-tax, Bengal (1937) I.L.R. (1937) 1 Cal. 653; 5 I.T.R. 90; A.I.R. 1937 P.C. 36; 41 C.W.N. 385.

Mst. Draupadi v. Vikram (1939) I.L.R. 1939 Nag. 88.

Vedathanni v. Commissioner of Income-tax, Madras (1932) I.L.R. 56 Mad. 1; 63 M.L.J. 542; A.I.R. 1932 Mad. 733; 140 I.C. 70; 1 I.T.R. 70; 6 I.T.C. 267.

Case stated under Section '66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, C. P. and U. P.: (Miscellaneous Civil Case No. 86 of 1942).

STATEMENT OF CASE.

"In compliance with your Lordships' order*, dated the 4th October 1940, in Misc. Civil Cases Nos. 138 and 139 of 1937, I have the honour to submit, for your Lordships' decision, under Section 66 (3) of the Indian Income-tax Act, 1922 (hereinafter referred to as "the Act"), the question of law set out in paragraph 3 below and held by your Lordships to arise from the assessments for the years 1935-36 and 1934-35 made on Mst. Panna Bai, minor, widow of Sheo Ratan deceased, under the guardianship of Mst. Mula Bai, widow of Chunnial Nathmal, of Nandura, taluq Malkapur, district Buldana.

2. Facts of the case.—Up to and including the assessment for the year 1933-34, based on the income of the 'previous year' ended Dewali 1932, the assessments in this case were made in the status of a Hindu undivided family. The family was originally composed of Chunnial Lal, the Karta, and his wife Mst. Mula Bai. In the year 1933 Chunnial Lal died, leaving his widow Mst. Mula Bai surviving him. She, as his

* Printed infra at p. 159.

widow, adopted Sheo Ratan and the joint family property devolved on him. In 1934 Sheo Ratan also died and was survived by his widow Mst. Panna Bai (minor) and the other widow Mst. Mula Bai. No male issue was left by either Chunni Lal or Sheo Ratan and the family during the material period of time was composed of the said two widows only. On the death of Sheo Ratan, his widow Mst. Panna Bai succeeded to the entire estate under the Hindu law. In these circumstances, the Income-tax Officer assessed Mst. Panna Bai (who will hereinafter be referred to as "the assessee") in the status of an 'Individual' for the years 1935-36 and 1934-35. The assessment for the year 1934-35 was originally made under Section 23 (4) of the Act on an income of Rs. 1,02,805. The assessee applied unsuccessfully to the Income-tax Officer under Section 27. Her appeal to the Appellate Assistant Commissioner was also not successful. The Commissioner, however, in exercise of his powers under Section 33 of the Act, as it stood prior to the 25th January 1941, set aside the assessment. A fresh assessment was then made by the Income-tax Officer on an income of Rs. 69,027, which on appeal was reduced to Rs. 33,120. The assessment for the year 1935-36 was in the first instance made on an income of Rs. 1,02,624 under Section 23 (4) of the Act. The assessee applied to the Income-tax Officer under Section 27 of the Act for cancellation of the assessment. The Income-tax Officer accepted the application and cancelled the assessment as by this time the Commissioner's order under Section 33 in respect of the assessment year 1934-35 had been received by him. A fresh assessment was made by the Income-tax Officer for 1935-36 on an income of Rs. 87,601, which on appeal was reduced to Rs. 43,602.

The assessee thereafter filed two combined applications under Sections 33 and 66 (2) of the Act before my predecessor, asking him to revise the fresh assessment under Section 33 or, in the alternative, to make a reference to the High Court under Section 66 (2) on the basis of certain alleged questions of law framed by her. My predecessor refused both these requests and rejected the applications.

3. *Question of law.*—It was in these circumstances that the assessee applied to your Lordships for the issue of a mandamus under Section 66 (3) of the Act. In so far as the applications related to the merits of the assessments the matters in dispute have been concluded by your Lordships' order of the 4th October 1940.* Your Lordships, however, have been pleased to direct me to state a case and to refer the following question of law for your Lordships' decision:—

"Where a Hindu family consists of a daughter-in-law (the widow of the last surviving coparcener) and her mother-in-law (the widow of

* Printed *infra* at p. 159.

that last surviving coparcener's father), do they form a 'Hindu undivided family' within the meaning of that term as used in Section 55 of the Income-tax Act?"

This question is accordingly referred to your Lordships for decision under Section 66 (3) of the Act.

Copies of the following documents, which appear to be all that is necessary for the determination of the question of law referred are attached hereto as Exhibits:—

(1) Fresh assessment order, dated the 11th May 1936, for 1934-35—Exhibit A; (2) Appellate order, dated the 21st September 1936, against fresh assessment for 1934-35—Exhibit B; (3) Fresh assessment order, dated the 21st May 1936, for 1935-36—Exhibit C; (4) Appellate order, dated the 21st September 1936, against fresh assessment for 1935-36—Exhibit D; (5) Commissioner's order under Sections 33/66 (2), dated the 5th February 1937, for 1934-35—Exhibit E; (6) Commissioner's order under Sections 33/66 (2), dated the 5th February 1937, for 1935-36—Exhibit F; (7) Assessee's application to the High Court, dated the 14th August 1937, under Section 66 (3)—Exhibit G; (8) High Court's order, dated the 4th October 1940, under Section 66 (3)—Exhibit H.*

4. Commissioner's opinion.—It may be stated at the outset that the Hindu Women's Rights to Property Act, 1937, has no application as both Chuni Lal and the son Sheo Ratan adopted by his widow Mula Bai died before the commencement of that Act. The case is governed by the general Mitakshara law of inheritance. According to Section 34 (2) (ii) of Mulla's Hindu law "if the deceased was at the time of his death the sole surviving member of a coparcenary, the whole of his property including the coparcenary property will pass to his heirs by succession according to the order given in Section 43. According to Section 43, the widow is the heir, though to a limited extent, if there is no son, grandson or great grandson. The mother's position is much lower down on the list (7th) and although the widow Mula Bai may be entitled to maintenance as member of the Hindu undivided family she can inherit the property only after Mst. Panna Bai. In *Kalyanji's case*¹, their Lordships of the Privy Council held 'that it would not be in consonance with ordinary notions or with a correct interpretation of the law of the Mitakshara to hold that property which a man has obtained from his father belongs to a Hindu undivided family by reason of his having a wife and daughters. It would be much less in consonance with ordinary notions or with the law of the Mitakshara to hold that property inherited by the widow of the sole surviving male member belongs to a Hindu undivided family consisting of herself

* Printed infra at p. 159.

(1) (1937) 5 I.T.R. 90.

and the widowed mother of her late husband. As ruled by the Privy Council in another case (*Bijoy Gopal v. Krishna*¹), a widow or other limited heir is not a tenant-for-life, but is *the owner* of the property inherited by her, subject to certain restrictions on alienation, and subject to its devolving upon the next heir of the last full owner on her death. The whole estate is for the time vested in her, and she represents it completely. As held in that case "her right is of the nature of a right of property; her position is that of owner; her powers in that character are, however, limited; but.....so long as she is alive no one has any vested interest in the succession."

So far as the income is concerned, Section 177 of Mulla's Hindu Law lays down:

"A widow or other limited heir is not a trustee for the reversioners. She has absolute power of disposal of the income of the property inherited by her. She is not bound to save the income. She may spend the whole income upon herself, or give it away as she likes during her life."

Thus the position is that the sole owner of the income and corpus is Mst. Panna Bai and her mother-in-law Mst. Mula Bai, even if entitled to maintenance, is not a co-heir with Panna Bai. The former's position as regards income is identical to that of a sole surviving male member (prior to 1937) having female members entitled to maintenance. Applying to this position the test laid down in the following observation of their Lordships of the Privy Council in *Kalyanji Vithaldas v. Commissioner of Income-tax, Bengal* [1937] (5 I.T.R. 90, on p. 95) the conclusion is irresistible that the income is to be assessed in the status of individual, even if it were conceded for the sake of argument that she and her widowed mother-in-law between them form a Hindu undivided family.

"In an extra legal sense, and even for some purposes of legal theory, ancestral property may perhaps be described, and usefully described, as family property; but it does not follow that in the eye of the Hindu law it belongs save in certain circumstances, to the family as distinct from the individual. By reason of its origin a man's property may be liable to be divested wholly or in part on the happening of a particular event, or may be answerable for particular obligations, or may pass at his death in a particular way; but if, in spite of all such facts, his personal law regards him as the owner, the property as his property and the income therefrom as his income, it is chargeable to income-tax as his, *i.e.*, as the income of an individual."

My respectful opinion, therefore, is that the question referred should be answered in the negative.

(1) (1907) L.R. 34 I.A. 87, at pp. 91, 92.

5. As required by the prescribed rules, a copy of the draft statement of facts and question of law was sent to the assessee by registered post on the 31st December 1941, and she was asked to state within 14 days whether she accepted the statement of facts as correct or desired any amendments to be made therein. No reply has, however, been received from her."

Exhibit H.

The application of the assessee under Section 66 (3) of the Indian Income-tax Act (XI of 1922) requiring the Commissioner of Income-tax, C. P. and U. P., to state a case came up for hearing before Stone, C. J., and Clarke, J., and the learned Judges passed the following order on 4th October 1940.

"This order disposes of Miscellaneous Civil Cases Nos. 138 of 1937 and 139 of 1937.

These are two applications which seek an order calling upon the Commissioner of Income-tax to state a case. They are made under Section 66 (3) of the Income-tax Act, 1922. M. C. C. No. 138 of 1937 relates to the year of assessment of 1935-36 while M. C. C. No. 139 of 1937 relates to the Income-tax year 1934-35. Otherwise the points are substantially the same and the applicants are the same and are the widow of one Sheoratan and the widow of Chunnilal Nathmal. Chunnilal Nathmal was a person who carried on money-lending-pawn-broking business together with other activities and he died in 1933 leaving the 2nd applicant, Mst. Mula Bai surviving him. She, as his widow, adopted to him Sheoratan who in turn died in 1934 leaving behind him his widow the 1st applicant, Mst. Panna Bai, who has been at all material times a minor. The Income-tax authorities appear in the past to have had a good deal of trouble with Chunnilal Nathmal and some of that trouble appears to have lived on after his death. Their difficulty has been to ascertain what is the true income assessable to income-tax. The Assistant Commissioner came to the conclusion that there had been suppressions so that the books which were placed before the Income-tax authorities as representing the business did not tell the true story and in particular he came to the conclusion that loans to the extent of 4½ lakhs of rupees had been kept out of the books and that had they been put in the books that would have shown an increase in income of Rs. 31,500. Then apparently the assessee filed affidavits and the Income-tax Officer appears to have been satisfied that no interest had been received in respect of those sums in respect of the accounting year. This finding was accepted by the Assistant Commissioner of Income-tax but he, as we think very rightly, concluded that books that left out of account 4½ lakhs and

kept by a business that was showing a total income of Rs. 2,593 for the year of assessment were not reliable books.

It is said that the Assistant Commissioner of Income-tax had nothing whatever to go upon in arriving at that conclusion of fact. To us it appears clear that he had very weighty material to go upon. The books before him did not refer at all to what must have been a very considerable part of the business. It is said that the Income-tax authorities knew all about this because they had accepted these books in the past and had been told and accepted the assurance that the books showed interest payments correctly whenever they were received from these loans. That, in our opinion, does not entitle the assessee who puts forward books of this kind before the Income-tax authorities to demand that those books should be accepted as correctly representing the position. The Assistant Commissioner observes as follows :—

“Admittedly loans of nearly four and half lacs to the above-named persons of Khandwa are not to be found in the Nandura or Bombay books and so also there is no mention in them of the deposit with Sadasukh Gambhirmal. It is, therefore, highly probable that the assessee has advanced similar loans to others without keeping any record of them in his accounts. There may be a record somewhere, but so far as the income-tax proceedings are concerned nothing has been produced. It is urged that though these accounts do not exist in the ledgers, the assessee has been showing them every year in the returns and returning such interest as was received in any year, and therefore, these are no omissions. I think the argument has only to be stated to expose its futility. It is a clear confession of the incompleteness of the accounts and the very fact that transactions involving lakhs of rupees do not find a place in the books takes away considerably from their reliability and evidentiary value.”

We regard that as a studied understatement and certainly do not think that it goes too far. It is a finding based on evidence and it is a conclusion, in our opinion, that raises no point of law. Neither does it raise a point of law that the Assistant Commissioner of Income-tax proceeds thereafter on the basis of Section 13 proviso of the Income-tax Act. Having come to the conclusion that the books are not regularly kept he does the best he can to estimate what the income is. He gives the assessee, as it appears to us, every possible allowance. In our view therefore there is no reason at all for him to state a case so far as this part of the application is concerned.

The application, however, raises another point which is a point of law and can be stated thus : Where, as here, the family has reduced down to the widow of the last surviving coparcener and her mother-in-law,

widow of that last surviving coparcener's father, do they form a Hindu undivided family within the meaning of that term as used in Section 55 of the Income-tax Act ? The point is one, in our opinion, of law and we apprehend that a case would have been stated on this point of law had the Commissioner of Income-tax not considered that the matter was not open not having been raised before the Assistant Commissioner. In our opinion the fact that it was not clearly raised should not shut out a point of this kind if no fresh facts are required in order fairly to raise the point and if there is no surprise, and in so saying we rely on the observations of Atkin, L.J., (as he then was) in *Attorney-General v. Aramayo and Others*¹, that "if the point of law or the erroneous nature of the determination of the point of law is apparent upon the case as stated and there are no further facts to be found, it appears to me that the Court can give effect to the law."

We, therefore, grant the application so far as the question raised in clause (i) of paragraph 5 is concerned and reject it so far as clauses (ii) and (iii) of paragraph 5 are concerned. The question formulated in paragraph 5 (1) will be somewhat extended. The question will be re-drafted to read as follows :—

"Where a Hindu family consists of a daughter-in-law (the widow of the last surviving coparcener) and her mother-in-law (the widow of that last surviving coparcener's father), do they form a 'Hindu undivided family' within the meaning of that term as used in Section 55 of the Income-tax Act ?"

R. K. Rao and V.K. Rajwada, for the assessee.

R.B.D.N. Choudhari, for the Commissioner.

The judgment of the Court on the Reference of the Commissioner under Section 66 (3) of the Income-tax Act was as follows :—

JUDGMENT.

In compliance with this Court's order dated 4th October 1940 in Miscellaneous Civil Cases Nos. 138 and 139 of 1937 the Commissioner of Income-tax of Central and United Provinces has submitted for this Court's decision under Section 66 (3) of the Indian Income-tax Act of 1922 the question of law set out below :—

"Where a Hindu family consists of a daughter-in-law (the widow of the last surviving coparcener) and her mother-in-law (the widow of that last surviving coparcener's father), do they form a 'Hindu undivided family' within the meaning of that term as used in Section 55 of the Income-tax Act ?"

2. The facts are that up to and including the assessment for the year 1933-34 based on the income of the previous year ended Diwali

(1) (1925) 9 Tax Cas. 445, at 497.

1932 the assessments in this case were made in the status of a Hindu undivided family. The family was originally composed of Chunnilal and his wife Mt. Mulabai. Chunnilal died in the year 1933 survived by the widow Mt. Mulabai who after her husband's death adopted one Sheoratan. He also died in 1934 leaving behind his widow Mt. Pannabai (Minor) but no son with the result that the family now consists of Mt. Pannabai, the daughter-in-law, and Mt. Mulabai, the mother-in-law. The Income-tax Officer assessed Mt. Pannabai in the status of an individual for the years 1934-35 and 1935-36. The Commissioner of Income-tax upheld the Income-tax Officer's order assessing Mt. Pannabai in the status of an individual and declined to make a reference to the High Court under Section 66 (2) of the Income-tax Act for its decision, whereupon the assessee obtained an order from this Court on 4-10-40.

3. The main argument on behalf of the assessee is that she and her mother-in-law who is entitled to maintenance as a member of the joint family, constitute a Hindu undivided family and consequently that the assessments should have been on the footing of a Hindu undivided family. Reliance was placed on behalf of the assessee on *Vedathanni v. Commissioner of Income-tax, Madras*¹, *Commissioner of Income-tax, Bombay v. Laxminarayan*², *Mst. Draupadi v. Vikram*³ and *Bajirao v. Ramakrishna*⁴, for the proposition that a Hindu joint family may consist of only female members. The two Nagpur cases are not in point as the questions there were dealt with purely as those arising under Hindu law and in no way related to the Income-tax Act. In *Vedathanni v. Commissioner of Income-tax, Madras*¹, the question was whether the maintenance and arrears of maintenance received by a widow of a member of a joint family was exempt from taxation under Section 14 (1) and other sections of the Indian Income-tax Act (XI of 1922). In that case there were some observations made that there could be a joint family with a single member provided that there were other members entitled to maintenance from the estate. In *Commissioner of Income-tax, Bombay v. Laxminarayan*² the joint family was composed of an assessee, his father, mother and wife. They were possessed of ancestral property which on the death of the father devolved on the assessee by survivorship and thereafter the assessee, his mother and wife continued to live as members of an undivided family. It was held that the income of the assessee should be taxed as an income of a Hindu undivided family for the purposes of super-tax under Section 55 of the Indian Income-tax Act, 1922.

(1) (1932) I.L.R. 56 Mad. 1 ; 1 I.T.R. 70. (3) (1939) I.L.R. 1939 Nag. 88.

(2) (1935) I.L.R. 59 Bom. 618; 3 I.T.R. 367. (4) (1941) I.L.R. 1941 Nag. 707.

4. Both these cases were considered by their Lordships of the Privy Council in *Kalyanji Vithal Das v. Commissioner of Income-tax, Bengal*¹, which in our opinion concludes the question raised in this case. In that case the business was begun by two separated brothers Moolji and Purshottam and one Kalyanji, a stranger, and their contribution to the capital was not from the ancestral funds. In 1939 Moolji made gifts of capital to each of his sons by his first wife, Kanji and Sew Das. Kanji and Chatur Bhuj, the brother of Kalyanji, were taken into the partnership. In 1930 Sew Das, Moolji's son, and Champsi, Kalyanji's brother, were also admitted in the firm as partners. The interest of Kanji and Sew Das was a gift from their father Moolji and that of Chatur Bhuj a gift from his brother Kalyanji. Moolji, Purshottam and Kalyanji each had son or sons from whom they were not divided. Their Lordships pointed out that the income from the firm received by each of them was clearly separate and self-acquired property of the partner and that as it was not thrown into the common stock it could not be regarded as an income of the joint family. It was therefore held that Moolji, Purshottam and Kalyanji were liable to be assessed as individuals and not as a Hindu undivided family.

5. While dealing with the cases of Kanji and Sew Das, sons of Moolji, their Lordships assumed that their interest in the firm, which was obtained from gift of their father Moolji, was ancestral property so that, if either had had a son, the son would have taken an interest therein by birth. Then their Lordships had to consider the question, "Does then the existence of a wife, or of a wife and daughter, make it income of a Hindu undivided family rather than income of the individual partner?" Their Lordships answered the question in the negative on the ground that a man's wife and daughter are entitled to be maintained by him out of his separate property as well as out of property in which he had a coparcenary interest, but the mere existence of a wife or daughter does not make ancestral property joint. Their Lordships made it clear that though the word "interest" might be used of a wife's or daughter's right to be maintained nevertheless that does not divest or impair the father's ownership of the joint property whether that property is self-acquired or ancestral property belonging to himself alone.

6. Their Lordships further pointed out that the main question for consideration for the purpose of Section 55 of the Income-tax Act is not whether the assessee, his wife and daughter or other individuals entitled to maintenance constitute a Hindu undivided family but whether the income of the assessee is the income of the family and disapproved of the view taken by the Bombay High Court in *Commissioner*

1932 the assessments in this case were made in the status of a Hindu undivided family. The family was originally composed of Chunnilal and his wife Mt. Mulabai. Chunnilal died in the year 1933 survived by the widow Mt. Mulabai who after her husband's death adopted one Sheoratan. He also died in 1934 leaving behind his widow Mt. Pannabai (Minor) but no son with the result that the family now consists of Mt. Pannabai, the daughter-in-law, and Mt. Mulabai, the mother-in-law. The Income-tax Officer assessed Mt. Pannabai in the status of an individual for the years 1934-35 and 1935-36. The Commissioner of Income-tax upheld the Income-tax Officer's order assessing Mt. Pannabai in the status of an individual and declined to make a reference to the High Court under Section 66 (2) of the Income-tax Act for its decision, whereupon the assessee obtained an order from this Court on 4-10-40.

3. The main argument on behalf of the assessee is that she and her mother-in-law who is entitled to maintenance as a member of the joint family, constitute a Hindu undivided family and consequently that the assessments should have been on the footing of a Hindu undivided family. Reliance was placed on behalf of the assessee on *Vedathanni v. Commissioner of Income-tax, Madras*¹, *Commissioner of Income-tax, Bombay v. Laxminarayan*², *Mst. Draupadi v. Vikram*³ and *Bajirao v. Ramakrishna*⁴, for the proposition that a Hindu joint family may consist of only female members. The two Nagpur cases are not in point as the questions there were dealt with purely as those arising under Hindu law and in no way related to the Income-tax Act. In *Vedathanni v. Commissioner of Income-tax, Madras*¹, the question was whether the maintenance and arrears of maintenance received by a widow of a member of a joint family was exempt from taxation under Section 14 (1) and other sections of the Indian Income-tax Act (XI of 1922). In that case there were some observations made that there could be a joint family with a single member provided that there were other members entitled to maintenance from the estate. In *Commissioner of Income-tax, Bombay v. Laxminarayan*² the joint family was composed of an assessee, his father, mother and wife. They were possessed of ancestral property which on the death of the father devolved on the assessee by survivorship and thereafter the assessee, his mother and wife continued to live as members of an undivided family. It was held that the income of the assessee should be taxed as an income of a Hindu undivided family for the purposes of super-tax under Section 55 of the Indian Income-tax Act, 1922.

(1) (1932) I.L.R. 56 Mad. 1 ; 1 I.T.R. 70. (3) (1939) I.L.R. 1939 Nag. 88.

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6. Their Lordships further pointed out that the main question for consideration for the purpose of Section 55 of the Income-tax Act is not whether the assessee, his wife and daughter or other individuals entitled to maintenance constitute a Hindu undivided family but whether the income of the assessee is the income of the family and disapproved of the view taken by the Bombay High Court in *Commissioner*

(1) (1937) I.L.R. (1937) 1 Cal, 653 ; 5 I.T.R. 90.

of *Income-tax, Bombay v. Laxminarayan*¹, that the income of an assessee having wife and mother constituting a Hindu undivided family was the income of the family. With reference to *Vedathanni v. Commissioner of Income-tax, Madras*², their Lordships observed that it did not cover the question arising under Section 55 of the Income-tax Act.

7. The test as laid down by their Lordships of the Privy Council in the above mentioned case is whether the income received by an assessee is exclusively his own or the income of the joint family. If the income is his individual income and not of a Hindu undivided family he would rightly be assessed as an individual. This is precisely the case here. The assessee is the sole owner of the property which has devolved on her on the death of her husband. That property may be joint property and she and her mother-in-law may constitute in a broad sense a Hindu undivided family but the income she receives from the property can in no way be regarded as an income of the family. As pointed out by their Lordships of the Privy Council in *Bijoy Gopal Mukerji v. Krishna Mahishi Debi*³, a widow on whom devolved the property of her husband is the owner of the property and that so long as she is alive no one has any vested interest in the succession. As Pannabai is the sole owner of the property and the entire income of the property belongs to her, the income is liable to be assessed as an income of an individual and not as an income of the joint family notwithstanding that it is subject to the right of maintenance in favour of her mother-in-law.

8. Our answer to the question therefore is that the daughter-in-law and mother-in-law do not form a Hindu undivided family within the meaning of that term as used in Section 55 of the Income-tax Act, *i.e.*, in relation to the income. Counsel's fee Rs. 50.

Reference answered accordingly.

[IN THE NAGPUR HIGH COURT.]

LUKHMANJI AND ANOTHER

v

COMMISSIONER OF INCOME-TAX, C.P. AND U. P.

GRILLE, C. J.

December 24, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 26A—FIRM—APPLICATION FOR REGISTRATION—BROTHERS CARRYING ON BUSINESS IN

(1) (1935) I.L.R. 59 Bom. 618; 3 I.T.R. 367.

(2) (1932) I.L.R. 56 Mad. 1; 1 I.T.R. 70.

(3) (1907) 34 Cal. 329; 34 I.A. 87.

PARTNERSHIP AFTER THEIR FATHER'S DEATH—SHARES NOT SPECIFIED AND HOUSEHOLD AND OTHER EXPENSES DEBITED TO FIRM—REFUSAL OF REGISTRATION—VALIDITY.

Two brothers after their father's death entered into a partnership. The deed did not specify their shares but simply stated that they were equally interested and further provided that all household expenses and expenses for any other purpose incurred by any member of either partner's family should be debited to the firm. The partners admitted that there had been no change in the business after their father's death and that it was to be carried on exactly as it had been during their father's time. The Income-tax authorities refused registration on the ground that no partnership in fact existed :

Held, that the question for decision was a question of fact and there was evidence on which the Income-tax authorities were entitled to reach the decision that the partnership was not a real partnership and to refuse registration.

Commissioner of Income-tax, Burma v. Seth Mangoomal Lunidasingh [1939] (7 I.T.R. 208 ; A.I.R. 1939 Rang. 178) distinguished.

Cases referred to :—

Bishweswarlal Brijlal, In re (1930) I.L.R. 57 Cal. 1336 ; 4 I.T.C. 365.

Commissioner of Income-tax, Burma v. Seth Mangoomal Lunidasingh (1939) 7 I.T.R. 208 ; 1939 Rang. 532 ; 182 I.C. 278 ; A.I.R. 1939 Rang. 178.

Hafiz Abdul Ghafoor v. Commissioner of Income-tax, C. P. and U. P. (1939) 7 I.T.R. 625 ; I.L.R. 1940 Nag. 200.

Mulla Fida Ali Sultan Ali v. Commissioner of Income-tax, C. P. & U. P. (1937) 5 I.T.R. 615.

Application under Section 66 (3) of the Indian Income-tax Act (XI of 1922) : (Miscellaneous Civil Case No. 86 of 1940).

A. V. Khare and M. B. Pendharker, for the assessee.

R. B. D. N. Choudhari, for the Commissioner.

ORDER.

The applicants sought to have themselves registered as a firm under the provisions of the Indian Income-tax Act, and their application was refused by the Income-tax Officer, Khandwa. The Appellate Assistant Commissioner of Income-tax, Jubbulpore, rejected their appeal and this order was confirmed by the Commissioner of Income-tax, Central and United Provinces. The applicants have applied in this Court asking that the Commissioner of Income-tax should be called on to state a case, and notice has been issued to that officer to show cause why he should not do so. An appearance has been made on his behalf.

2. The Income-tax authorities have considered that the deed of partnership drawn up between the two applicants and which was put forward as a basis for registration is a sham and that in fact no partnership exists. The partnership deed in question runs as follows:—

“This indenture made on 30th day of August 1938 witnesseth as follows:—

1. That the parties (1) Seth Likhmanji alias Nanabhai and (2) Seth Hasanali son of Seth Jiwaji Bohras, merchants residents of Khandwa along with their sister Mst. Ratanbai w/o Seth Adamji of Majmadi Junagadh State and mother Mst. Mannubai inherited the business in the year 1917 formerly carried on by Seth Jiwaji son of Seth Amiji under the name and style of “Jiwaji Amiji” at Khandwa as Seth Jiwaji died at the close of 1917.

2. That the claims of sister Mst. Ratanbai and mother Mst. Mannubai were settled in 1918 and since 5th April 1918 Seth Likhmanji alias Nanabhai and Seth Hasanali carry on the business under the name and style ‘Jiwaji Amiji’ in partnership wherein they are equally interested.

3. That the partnership is registered according to law.

4. That the partnership owns properties such as press, houses, vacant sites and money-lending and the like.

5. That for business, proper and regular accounts shall be maintained and shall be open to all inspection, profit and loss statement shall be drawn up in ledger every year say at Diwali. This shall be done if either considers it necessary. That out of mutual love and affection the partners hereunto hereby agree that the expenses of the business, household management and any other purpose by either partner or any member of his family shall be debited to the firm without regard to the unequal burden on each.

6. That each of the partners has voice in the business and shall show due diligence in its management and can withdraw at any time by taking not only the usufruct but also his share in the capital.

7. That each of the partners does effectively represent the firm and can sue or be sued and can refer any matter in dispute to arbitration.

8. That Nazarali son of Seth Likhmanji is working in the shop and shall be admitted to partnership to the extent of -/4/- on 24-10-33 on receipt of half share from his father that at present he is not entitled to any remuneration.

9. That both the partners are alive to the extent of their capital but intentionally do not want others to know it and so the extent is not disclosed here or in the account books.”

The conclusion of the Income-tax authorities is based principally on the circumstances revealed by clause 5 of that document.

3. It has been amply established that whether a partnership exists or not is a question of fact within the power of the Commissioner of Income-tax to determine on the evidence placed before him. The only ground this Court could have for interference would be that there was no evidence before the Commissioner of Income-tax on which a decision adverse to the applicants could be based. The question has been decided more than once in this High Court, vide *Mulla Fida Ali Sultan Ali v. Commissioner of Income-tax, C.P. and U.P.*¹ and *Hafiz Abdul Ghafoor v. Commissioner of Income-tax, C. P. and U. P.*² Reference may also be made to *In re Bishweswarlal Brigla*³.

4. The evidence in this case consists of the terms of the partnership deed itself and the testimony of the two applicants. It is admitted that the business is exactly as it was in their father's time, that there has been no change, and that they are not aware of the value of the whole estate as it has not been ascertained at any time since their father's death 20 years previously, and that when their mother and their sister, the only other members of the family when their father died, were given their share and their share was not given out of any of the estate property but out of ornaments which the brothers took from their wives. Incidentally this is at variance with clause 9 of the partnership deed which states that "both the partners are alive to the extent of their capital." It is apparent that the brothers continue to hold everything in common as they have done during the last 20 years during which time they have been assessed as an association of individuals. It is of some significance, that the partnership deed does not give their shares as 8 annas each but merely states that they are equally interested, and the explicit statement in clause 5 that all household expenses and expenses for any other purpose whatever shall be debited to the firm is certainly sufficient evidence on which the Commissioner of Income-tax could come to the conclusion that there was no genuine partnership and that, as the applicants themselves admit, business was to be carried on exactly as it had been for the past 20 years. The effect of this piece of evidence, or rather the admissibility of its consideration by the Commissioner of Income-tax, is attacked by the applicants on the authority of a decision of the Rangoon High Court, *Commissioner of Income-tax, Burma v. Seth Mangoomal Lunidasingh*⁴. The report is of no assistance to the applicants. In the first place the Commissioner of Income-tax, Burma, did not dispute that there was a

(1) (1937) 5 I.T.R. 615.

(3) (1930) I.L.R. 57 Cal. 1336.

(2) (1939) 7 I.T.R. 625; I.L.R. 1940 Nag. 200. (4) (1939) A.I.R. 1939 Rang. 178; 7 I.T.R. 208.

genuine partnership, which is the point in issue here, but contended that, by reason of a clause in the deed of partnership whereby the remuneration of the partners was to vary in accordance with the time devoted by the partners to the business, the shares could not be specifically defined. It was held that a share did not mean the same thing as net receipts and that where the partnership is genuine (and as I pointed out the fact was not disputed) the shares as set out in the partnership deed were not affected by a method of computation of those receipts, specifically introduced into a genuine deed, made for the purpose of adjusting remuneration due to a partner consequent on his absence from duty with the firm. This is a very different matter from a condition that all expenses, domestic or otherwise, incurred by any member of either partner's family shall be debitable without exception to the firm. The evidence of the intention to continue in a state of jointness analogous to that of a Hindu joint family is none the less evidence for being openly stated in a supposed deed of partnership than if it were concealed and had to be ascertained *aliunde*.

5. The question for decision is a question of fact and there is evidence on which the Commissioner of Income-tax was entitled to reach the decision that the partnership was not a real partnership and to refuse registration. The result is that the application fails and is dismissed with costs.

Application dismissed.

[IN THE NAGPUR HIGH COURT.]

SETH GOPALDAS

v.

COMMISSIONER OF INCOME-TAX, C. P. AND U. P.

GRILLE, C. J., and VIVIAN BOSE, J.

October 5, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 66 (3)—REFERENCE—
WHETHER GIFT IS REAL AND BONA FIDE—QUESTION OF FACT.

The question whether a certain gift is real and bona fide or nominal made in order to escape income-tax is a question of fact and such a question cannot therefore be referred.

Application under Section 66 (3) of the Indian Income-tax Act (XI of 1922): Miscellaneous Civil Cases Nos. 113 and 150 of 1942.

COMMISSIONER'S ORDER.

" This is an application under Sections 83 and 66 (2) of the Income-tax Act by Seth Gopal Das Bulakhi Das Mohta of Hinganghat arising

out of the assessment of his family for the year 1937-38 and the appellate order in respect thereof.

The same point is involved in the assessment for the year 1938-39 also and the applicant has filed an application under Sections 33 and 66 (2) of the Act in respect of that assessment as well. This order will govern both applications.

2. The applicant is the *karta* of a Hindu undivided family (composed of himself, his wife Mst. Ganga Bai *alias* Jetha Bai and their two minor sons named Ghanshyam Das and Purshottam Das) which carries on business in multifarious lines at different places and under various names and styles and also derives income from house property and securities. For the assessment year 1937-38, based on the income of the previous year ended Dewali 1936, the family was assessed by the Income-tax Officer, Wardha, under Section 23 (3) of the Act on a total income of Rs. 55,813. In this figure was included a sum of Rs. 10,140-8 being interest on capital standing (in the books of the business styled "R. S. Rekhchand Gopaldas Mohta Mills, Akola") to the credit of an account in the name of Mst. Ganga Bai *alias* Jetha Bai, wife of the applicant, which was disallowed by the Income-tax Officer. On appeal, the Assistant Commissioner of Income-tax upheld the Income-tax Officer's assessment in part; but in respect of the aforesaid sum of Rs. 10,140-8 (which is now in dispute) and another item no longer in dispute, he remanded the case to the Income-tax Officer for further investigation and disposal according to law.

The Income-tax Officer accordingly re-investigated the claim of the applicant for the allowance of the aforesaid sum of Rs. 10,140-8 in the assessment for 1937-38 and for a similar allowance of a sum of Rs. 13,367-4 in the assessment for 1938-39. He found that the account in the name of Mst. Ganga Bai *alias* Jetha Bai was brought into existence for the first time on 26-12-1935, on which date a sum of Rs. 2,25,001 was credited to this account by appropriation out of, and with a corresponding debit of this amount to, the Profit and Loss account. After considering a written statement filed by the applicant and examining his agent and hearing his Advocate, the Income-tax Officer, for the reasons fully detailed in his order, dated the 23rd January 1939, for the assessment year 1938-39, held that there was "no transfer of money much less a gift" in favour of the lady and that consequently the so-called interest on borrowed capital was really interest appropriated by the applicant's family to itself on the family's own capital and not an admissible deduction under the Act. He therefore disallowed the two items of interest in the assessment for 1937-38 and 1938-39.

On further appeal by the applicant, the Assistant Commissioner found that, though such gifts were common among the wealthy Mar-wari community and other gifts had been made in the past to other female members of this family itself, the past assessments made on the applicant's family indicated that the financial position of the family was not such as to justify the gift of so large an amount of money as Rs. 2,25,001 to the applicant's wife. He therefore held that the alleged gift was not genuine and the money still belonged to the family and that the two items of interest referred to were rightly disallowed in the assessments for 1937-38 and 1938-39.

It is in these circumstances that the applicant has filed before me the present applications under Sections 33 and 66 (2) of the Act, asking me either to revise the assessments for 1937-38 and 1938-39 by allowing a deduction of the sums of Rs. 10,140-8 and Rs. 13,367-4 respectively or, in the alternative, to refer the case to the High Court on the basis of certain questions said to be questions of law arising out of the appellate orders of the Assistant Commissioner.

3. The Assistant Commissioner accepted the proposition that a Hindu father is empowered to make reasonable gifts of affection to members of his family, but held in effect that the alleged gift in this case is not reasonable and is not a real gift but a mere device to evade income-tax. The only question which arises, therefore, is whether or not the alleged gift is reasonable and real. This is a pure question of fact and if there is material to support the Assistant Commissioner's finding no question of law will arise for reference to the High Court.

Now the applicant contended before the Income-tax Officer that the gift of Rs. 2,25,001 was out of *income* and not out of capital and the amount, as shown above, was actually debited to the Profit and Loss account. The Assistant Commissioner has shown in his appellate order that the income of the applicant's family in the recent past was not such as to enable him to make out of it a genuine gift of so large a sum as 2½ lakhs to his wife and the gift clearly cannot be called reasonable. It is true that in the year 1905 the father of the applicant made an alleged gift of Rs. 1,20,000 to his wife and that in the still more distant past the grand-father also made an alleged gift of Rs. 1,00,000 to his wife; but there is nothing to show that those gifts even were genuine. The tacit recognition of the gifts by the Department cannot be taken as conclusive proof of the fact. Further, even if those gifts were real and *bona fide* they do not prove that the present gift is so. Those gifts were made at a time when the original family was still undivided and the resources of the family were conceivably

greater than the resources of the present off-shoot family. The alleged gift made on the present occasion was certainly not capable of being made out of the comparatively slender income derived by the applicant's family in recent years. Furthermore, as explained in paragraph 225 of *Mulla's Hindu Law* (9th Edition) although a Hindu father has the power of making *within reasonable limits* gifts of ancestral movable property, such gifts must be for the purpose of performing "indispensable acts of duty and for purposes prescribed by texts of law, as gifts through affection, support of the family, relief from distress and so forth." It has already been shown that the alleged gift in this case is not within reasonable limits. It is also clear that it was not made for any of the purposes mentioned. The applicant's family consists of himself, his wife and their own minor sons and there are no other adult male members in the family with an interest in the ancestral property. There was therefore really no occasion for making any gift to the applicant's wife at all, let alone a gift of an unreasonable amount. The motive for making the gift ascribed by the applicant, *viz.*, to promote peace and harmony in the family, does not exist in fact. The applicant's sons are both minors and were not in a position to object to this arbitrary alienation of their patrimony and this casts a suspicion on the *bona fides* of the gift. Finally, there is no evidence of any kind beyond the mere entries in the books that a real gift was made to the applicant's wife in the sense that the money has passed from the joint ownership of the family to the sole ownership of the lady.

These facts, in my opinion, constitute sufficient material for the finding that the alleged gift is neither reasonable nor real and *bona fide*, but a mere device to evade income-tax payable by the family. This being so, no question of law arises for reference to the High Court under Section 66 (2) of the Act. Nor are there any grounds for interference with the assessments under Section 33.

4. The applications are dismissed."

The applications under Section 66 (3) coming on for hearing the Court passed the following Orders.

M. D. Khandekar, for the assessee in M. C. C. Nos. 113 and 150 of 1942.

ORDER.

(*Miscellaneous Civil Case No. 113 of 1942*)

The only question here is whether a certain gift was real and *bona fide* or nominal, made in order to escape income-tax. The finding is that it is not real. That is a pure finding of fact and no reference lies. The application is dismissed.

ORDER.

(*Miscellaneous Civil Case No. 150 of 1942*).

The only question here is whether a certain gift was real and *bona fide* or nominal, made in order to escape income-tax. The finding is that it is not real. That is a pure finding of fact and no reference lies. The application is dismissed.

Applications dismissed.

[IN THE BOMBAY HIGH COURT.]

DINSHAW DARABSHAW SHROFF

v.

COMMISSIONER OF INCOME-TAX, CENTRAL.

BEAUMONT, C.J., and KANIA, J.

September 16, 1942.

INCOME-TAX—WRIT OF CERTIORARI—POWER OF HIGH COURT TO ISSUE WRIT CHALLENGING VALIDITY OF INCOME-TAX ASSESSMENT—INCOME-TAX PROCEEDINGS—NATURE OF—WHETHER PARTNER OF ASSESSEE OR OFFICIAL SUPERIOR OF INCOME-TAX OFFICER CAN BE PRESENT AT INQUIRY—INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 37, 54, GOVERNMENT OF INDIA ACT, 1935, SEC. 226.

The High Court has no power, in view of Section 226 of the Government of India Act, 1935, to issue a writ of certiorari to challenge the validity of an income-tax assessment purporting to be made under the Indian Income-tax Act, 1922.

Obiter.—In view of the terms of Section 54 of the Income-tax Act, which require that all proceedings under the Act should be treated as confidential, an Income-tax Officer when dealing with an assessment is not justified in allowing the assessee's partner, who is not concerned with the assessment, to take part in the proceedings.

Although an Income-tax Officer making an assessment is not strictly acting as Court of law, it is clear from Section 37 that he is acting in a quasi judicial capacity, and he ought to conform to the more elementary rules of judicial procedure, and in particular to conduct the case himself, and not allow somebody else, even his superior officer, to take the conduct out of his hands.

It is grossly improper for any other revenue officer, particularly the official superior of the Income-tax Officer (i.e., Inspecting Assistant Commissioner), to appear in an assessment proceeding and to put questions directly to the assessee or to put them indirectly through the mouth of the Income-tax Officer who is conducting the inquiry.

K.R.M.T.T. Thyagaraja Chettiar v. The Collector [1936] (4 I.T.R. 56) followed; *Ramjidas Mahaliram, In re* [1936] (4 I.T.R. 25) distinguished; *Haji Rahemtulla v. Secretary of State* [1925] (27 Bom. L.R. 1507) doubted.

Cases referred to :

Alcock Ashdown & Co. v. Chief Revenue Authority, Bombay (1923) I.L.R. 47 Bom. 742,

Haji Rahemtulla v. Secretary of State (1925) 27 Bom. L.R. 1507.

K. R. M. T. T. Thyagaraja Chettiar v. The Collector of Madura (1936) 4 I.T.R. 56.

Ramjidas Mahaliram, In re (1936) 4 I.T.R. 25; 62 Cal. 1011.

O. C. J. Miscellaneous No. 86 of 1942.

The facts of the case appear sufficiently from the judgment of Beaumont, C.J.

Sir Jamshedji Kanga with *R. J. Kolah*, for the assessee.

M. C. Setalvad with *G. N. Joshi*, for the Commissioner.

JUDGMENT.

BEAUMONT, C. J.—This is a petition presented to the Court by an assessee making respondents the Commissioner of Income-tax, Central, the Income-tax Officer, Section III, and the Inspecting Assistant Commissioner, Central, and the relief asked for is that this Court may be pleased to issue a writ of certiorari against the respondents calling upon them to send up the records of the assessment of the petitioner for the year 1937-38 for the purpose of inquiring into the legality of the assessment order passed by respondent No. 2 on February 16, 1942, and the proceedings in respect of which such order was passed and to quash the same. Further relief asked for is that the Commissioner of Income-tax, Central, the Inspecting Assistant Commissioner, and the Income-tax Officer, Section III, Central, be ordered to forbear from (i) taking or continuing any proceedings for the purpose of levying any penalty under the provisions of Section 28 or otherwise; (ii) taking or continuing any proceedings or exercising any jurisdiction or passing any orders in respect of or arising out of the said assessment order or assessment proceedings under the Indian Income-tax Act; and (iii) exercising any jurisdiction or passing any orders in respect of the premises. The further relief seems to be consequential upon or ancillary to the primary relief asked for, namely, the issue of a writ of certiorari.

The grounds on which the petitioner bases his claim are two. First, that the assessment made against him for the year 1937-38 was made by an Income-tax Officer who had no jurisdiction to assess him, since the petitioner's assessment for that year had never been legally transferred to the officer who made the assessment, that is Mr. Shah; and, secondly, that the proceedings before the Income-tax Officer were so grossly irregular as to offend against the principles of natural justice—

On those two grounds, it is said that we ought to send for the record, and quash the assessment.

The Crown have taken a preliminary objection that the Court has no jurisdiction to issue a writ of certiorari in a case of this nature by reason of Section 226 of the Government of India Act, 1935, and Section 54 or Section 67 of the Indian Income-tax Act, 1922. For the purpose of considering the preliminary objection, we must assume that the petitioner's contentions are justified, and particularly that his case had not been legally assigned to the Income-tax Officer who made the assessment.

Section 226 of the Government of India Act, 1935, enacts: "Until otherwise provided by Act of the appropriate Legislature, no High Court shall have any original jurisdiction in any matter concerning the revenue, or concerning any act ordered or done in the collection thereof according to the usage and practice of the country or the law for the time being in force."

It is well-known that the provision has appeared in many previous Acts, and has its origin historically in the disputes between Warren Hastings as Governor-General of Bengal and Sir Elijah Impey as Chief Justice. However, we are not concerned with the reasons for the enactment, and we have to carry out the law as we find it. It has been held by the Privy Council in *Alcock, Ashdown and Company v. Chief Revenue Authority, Bombay*¹ that an order of a High Court directing a revenue officer to carry out his statutory duty would not involve the exercise of original jurisdiction in any matter concerning the revenue, and if there were any illegalities relating to the carrying out of this assessment, it may well be that we might have interfered at an earlier stage. But the difficulty here is that an assessment order has in terms been made, even if by the wrong officer, and we are asked to send for the record, and satisfy ourselves whether the order is legal or illegal, and if illegal, to quash it, and in effect stay execution upon it. It seems to me impossible to say that in so acting we should not be exercising original jurisdiction in a matter concerning the revenue. There is no doubt that the issue of a writ of certiorari is within the competence of this Court in a proper case, and that such issue is in exercise of the original jurisdiction of this Court. But we have been referred to no authority in support of the proposition that a writ of certiorari can properly issue to challenge the validity of an income-tax assessment purporting to be made under the Indian Income-tax Act.

We are referred to a decision of a single Judge of the Madras High Court in *K.R.M.T.T. Thyagaraja Chettiar v. The Collector*², in which

(1) (1923) L.R. 50 I.A. 227.

(2) (1936) 4 I.T.R. 56.

it was held that the Court could not issue a writ of certiorari to prevent the execution of an alleged illegal assessment order. That case seems to me to be an authority directly in point. There is another case in the same volume in *Ramjidas Mahaliram, In re*¹, in which a single Judge of the Calcutta High Court intimated the view that a writ of certiorari could issue in order to challenge the legality of an income-tax assessment. But in the course of that proceeding, the relief claimed was limited to a writ of prohibition ; so that the learned Judge's observations as to a writ of certiorari, were *obiter dicta* only ; and as eventually no writ, even of prohibition, was issued, the case is not a direct authority. In my opinion, the decision of the Madras High Court was right, and it is not open to this Court, in view of Section 226 of the Government of India Act, to call for the record of the Income-tax Department in order to satisfy ourselves that this assessment was legal.

It is stated in *Lord Halsbury's Laws of England*, Vol. 9. para. 1446, at p. 854, in dealing with the writ of certiorari that—

“The writ can only be issued in respect of matters which are within the jurisdiction of the High Court of Justice ; for proceedings will not be removed into the superior Court unless they are capable of being determined there.”

It seems to me clear that we are not capable of determining in this Court any question as to the validity of an assessment to income-tax under a writ of certiorari. We are not concerned with any matter except the claim to a writ of certiorari and consequent relief. Assesseees have various rights under the Indian Income-tax Act, right of appeals and other rights, with which we are not concerned in this case ; nor are we concerned to consider whether the assessee has any such remedy as was allowed in *Haji Rahemtulla v. Secretary of State*², where the Court made a declaration of nullity against an assessment order, and even ordered refund of the money, though the latter relief might be difficult to reconcile with later decisions of the Privy Council. Our decision is limited to holding that we have no power to issue a writ of certiorari in the circumstances of this case. As we think that the relief claimed is barred by Section 226 of the Government of India Act, 1935, it is not necessary to consider whether Section 54 or 67 of the Indian Income-tax Act affords a further bar.

As the preliminary objection prevails, it is not necessary to deal with the merits of the petitioner's case and I do not propose to say anything upon the question whether the Income-tax Officer who made

(1) (1936) 4 I.T.R. 25.

(2) (1925) 27 Bom. L.R. 1507.

the assessment was empowered to do so; but it is, I think, desirable to say something about the second ground relied on by the petitioner namely, that there were such irregularities in the assessment as to infringe the principles of natural justice. It seems necessary to say something on that question, because the Income-tax Officers have justified in their affidavits the course which was adopted. Their view of the matter is stated in para. 32 of the affidavit made by Mr. Pais, Office Superintendent, to respondent No. 1, and it appears from his affidavit, as well as from the affidavit of the petitioner, that when the Income-tax Officer, Mr. Shah, was dealing with the assessment of the petitioner for the year 1937-38, he allowed the petitioner's partners to be present, one of them with his solicitor, and to take part in the proceedings, although they were not concerned with the assessment of the petitioner. It is, I think, difficult to justify that course in view of the terms of Section 54 of the Indian Income-tax Act, which require that all proceedings under the Act should be treated as confidential. An assessee may well desire that his partners should not know what return he has made under the Act. But a more serious irregularity was this. The Inspecting Assistant Commissioner, Central, who is alleged to be the superior officer of the Income-tax Officer making the assessment, was not only present when the assessment was made, but claimed the right to put questions to the assessee, and when that course was objected to, he said that he would put the questions through the mouth of the Income-tax Officer who was conducting the inquiry, and was an officer subordinate to him. Now, it seems to me that that procedure was grossly irregular. The competent revenue authorities, I will assume, had assigned the assessee's case to Mr. Shah. That is the Crown case, and I assume for the present purpose that it is correct. It was then the duty of Mr. Shah to make the assessment himself. If the authorities were not satisfied with the conduct of Mr. Shah, they could have removed him, and appointed some other officer, but there is nothing to show that they were dissatisfied with his conduct, and, in my opinion, it was grossly improper for any other Revenue Officer, particularly a superior officer, to appear in the proceedings, and in effect dictate to the Income-tax Officer to whom these proceedings had been transferred what questions were to be asked, and presumably what conclusion he was to arrive at. It would be as sensible to suggest that a High Court Judge can sit in a Subordinate Judge's Court, not as a spectator only, but as an active participant, and can direct the trial Judge, as a Judge subordinate to the High Court, how to conduct the trial. That is not the way in which proceedings of a judicial nature should be conducted. Although, no doubt, an Income-tax Officer making an assessment is,

not strictly acting as a Court of law, it is clear from Section 37 of the Indian Income-tax Act that he is acting in a *quasi judicial* capacity, and he ought to conform to the more elementary rules of judicial procedure, and in particular to conduct the case himself, and not allow somebody else, even his superior officer, to take the conduct out of his hands. It is desirable to make these observations, because, I have no doubt that, had an application been made to this Court, at an earlier stage of the proceedings, we should have interfered to prevent this irregularity, and ordered Mr. Shah to carry out his duty in a proper manner. However, these observations are by way of caution only, and the actual decision of this Court is that we have no jurisdiction to issue a writ of certiorari in a case of this nature.

We must, therefore, discharge the rule with costs.

KANIA, J.—I agree. Two points arise for consideration on this petition. The first is whether prayer (1) could be granted in face of Section 226 of the Government of India Act of 1935. In that connection it must be remembered that the order of assessment has been made, and no question as to what the Court would have done to stop the order of assessment, on the ground of want of jurisdiction or irregularity amounting to miscarriage of justice in the conduct of the inquiry, arises.

Section 226 of the Government of India Act prevents the exercise of original jurisdiction by this Court in any matter concerning the revenue, or concerning any act ordered or done in the collection thereof. The order of Mr. Shah made on February 16, 1942, on the face of it is an order directing the assessee to pay. The first prayer is asking the Court to call for the records of these proceedings and to quash that order. In view of the clear words of Section 226, I agree that it is not permitted to this Court to exercise such jurisdiction.

The question of irregular exercise of jurisdiction is apart from the question whether the Income-tax Officer had any jurisdiction at all. The question of stopping him from exercising a jurisdiction which is never vested in him is clearly arguable under the decision of the Privy Council in *Alcock, Ashdown & Co. v. Revenue Authority, Bombay*¹. But that case does not lend support to the argument of the petitioner that after an order of assessment is made, the Court has jurisdiction to set aside such order. In *Alcock Ashdown's case*¹ the Court was asked to direct the Commissioner to state a case, that is to perform a duty which the Court held was on him to perform. Conversely, under Section 45 of the Specific Relief Act, if an officer having no jurisdiction whatsoever was attempting

(1) (1923) 50 I.A. 227.

to act as if he had jurisdiction, the Court may restrain him from acting in that way. But no case has been pointed out which goes to the length of saying that an order in fact made by a revenue officer could be set aside under an application for a writ of certiorari. It is clear that without setting aside that order the Court cannot give the relief asked for in prayer (2), because the foundation of the second prayer is that the order should be set aside, and on that footing the Court should order the officer to prevent further steps being taken. If the Court has no jurisdiction to set aside the order of assessment, it is equally incompetent to issue a writ of certiorari or make a prohibitory order in respect of the enforcement of the order which it cannot set aside. In view of the clear words of Section 226, therefore, I agree that the Court is unable to grant to the petitioner the relief in the form asked in this petition. The petitioner, may, if he is so advised, and is entitled to, take steps under the Indian Income-tax Act by way of appeal, etc., or under other Acts to contest the validity of the order made, and refrain from payment.

Under Section 37 of the Indian Income-tax Act the proceedings are for certain sections of the Indian Penal Code, 1860, called "Judicial Proceedings." In the judgment of the learned Chief Justice just delivered, the question of how improperly the matter was conducted in the matter of re-assessment has been fully dealt with, and I do not propose to add anything to those observations. But this judgment must be clearly understood as not absolving the taxing authorities from meeting the contention of the petitioner in appropriate proceedings in respect of the inquiry made for re-assessment. The decision of this Court is only in respect of the two reliefs asked for in the present petition. By virtue of Section 226 of the Government of India Act as the Court considers that it is unable to entertain the present petition in the present form, the only order made is that the petition is dismissed. I agree, therefore, that the same should be dismissed with costs.

Petition dismissed.

[IN THE NAGPUR HIGH COURT.]

NAZAR ALI ISHABHAI

v.

COMMISSIONER OF INCOME-TAX, LUCKNOW.

GRILLE, C.J., and PURANIK, J.

January 29, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE AMENDMENT),
SEC. 66 (2), (3)—REFERENCE—APPLICATION TO COMMISSIONER TO STATE
CASE—DISMISSAL OF APPLICATION AND SUBSEQUENT WITHDRAWAL OF
DEPOSIT—APPLICATION UNDER SECTION 66 (3) TO HIGH COURT AFTER
MAKING FRESH DEPOSIT—COMPETENCY.

When the Commissioner of Income-tax refuses to state a case on the application of the assessee under Section 66 (2) of the Income-tax Act, the assessee is given the option of either withdrawing the application and getting back the money deposited or applying to the High Court within the time prescribed by Section 66 (3). If the assessee exercises the option of withdrawing the application and gets a refund of the fee deposited by him, he cannot apply to the High Court under Section 66 (3) or prosecute his application before it by making a fresh deposit.

Application under Section 66 (3) of the Indian Income-tax Act (XI of 1922): (Miscellaneous Civil Case No. 108 of 1942).

Fida Hussain, for the assessee.

R. B. D. N. Chaudhuri, for the Commissioner.

ORDER.

The petitioner filed an application under Section 66 (3) of the Indian Income-tax Act and prayed for a writ of mandamus on the Commissioner of Income-tax, C.P. and U.P., calling upon him to state the case and refer the same to the High Court for decision. On 10-8-42 this Court issued a notice to the Commissioner of Income-tax calling upon him to show cause why mandamus should not be issued. On service of this notice the Commissioner of Income-tax filed an application on the 16th November 1942 stating that the Commissioner of Income-tax refused to state the case when the applicant made an application before him under Section 66 (2) on 30th September 1941, and when a copy of that order was served on the assessee on 6-10-41 the assessee made an application on the 3rd November 1941 to Commissioner requesting him to permit him to withdraw his application under Section 66 (2) and praying for refund of the deposit of Rs. 100; the Commissioner acceded to the request of the assessee and ordered the

Income-tax Officer, Khandwa, to refund the deposit, which was eventually done. Under the circumstances, the Commissioner of Income-tax stated, the petitioner was not entitled to pursue his application for reference in the High Court.

2. The assessee admits that he did apply as stated by the Commissioner of Income-tax and has obtained Rs. 100 that he had deposited in the Income-tax Department. He, however, contends that after getting back the deposit he again deposited the same amount with the Commissioner and that he is entitled to continue his application for a reference under Section 66 (3). It was stated on his behalf that his application before this High Court under Section 66 (3) is independent of his remedy which he pursued before the Income-tax Commissioner and therefore the mere fact that he applied to the Income-tax Commissioner for withdrawing the application made before him and for refund of the money did not disentitle him to pursue his application.

3. Section 66 (2) of the Indian Income-tax Act before the amendment of 1939 permits any assessee who is dissatisfied with the order passed by the Income-tax authorities against him to apply to the Commissioner of Income-tax requesting him to refer to the High Court any question of law arising out of such order. This application has to be accompanied by a fee of Rs. 100. The Commissioner may thereupon refer the question raised or reject the application on the ground that it is barred by time or otherwise incompetent, or he may refuse to state the case. When the Commissioner refuses to state the case or rejects the application the assessee may within 30 days from the date on which he receives notice of the order by the Commissioner withdraw his application, and if he does so the fee paid is refunded. Section 66 (2) lays down :

"If, on any application being made under sub-section (2), the Commissioner refuses to state the case on the ground that no question of law arises, the assessee may within six months from the date on which he is served with notice of the refusal apply to the High Court, and the High Court, if it is not satisfied of the correctness of the Commissioner's decision, may require the Commissioner to state the case and to refer it, and, on receipt of any such requisition the Commissioner shall state and refer the case accordingly."

It will thus be seen that when the Commissioner refuses to state the case the assessee is given the option of either withdrawing the application and getting back the money deposited by him or applying to the High Court within the time prescribed above. It necessarily follows from this that if the assessee exercises the option of withdrawing the application and gets a refund of the fee deposited by him he

cannot apply to the High Court or continue his application before it. As the petitioner in this case has chosen the alternative of withdrawing his case for reference he is not entitled to prosecute his petition under Section 66 (3) of the Indian Income-tax Act. The petitioner stated before us that he had made a fresh deposit of Rs. 100. There is no provision of law under which such a fresh deposit can be made. It is clear from the section itself that if the applicant wanted to approach the High Court with a request to call upon the Commissioner to make a reference he ought not to have withdrawn the application before the Commissioner or got back his deposit.

4. In this view of the case the application filed before us fails and is dismissed. The applicant shall pay Rs. 75 as costs to the Income-tax Commissioner.

Application dismissed.

[IN THE MADRAS HIGH COURT.]

ANNAM VENKATAKUTUMBA RAO

v.

YENDURI VEERABHADRU AND OTHERS.

WADSWORTH and PATANJALI SASTRI, JJ.

October 6, 1942.

HINDU UNDIVIDED FAMILY—PARTITION—ASSESSMENT OF MANAGER TO INCOME-TAX IN IGNORANCE OF DIVISION—VALIDITY—DIVIDED MEMBER—WHETHER ASSESSED TO INCOME-TAX—WHETHER ENTITLED TO BENEFIT OF MADRAS AGRICULTURISTS' RELIEF ACT—INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 14 (1), 25A (3)—MADRAS AGRICULTURISTS' RELIEF ACT (IV OF 1938), SECS. 19, 3 (11), PROVISO A.*

Where a member of a joint Hindu family became divided from his uncle as a result of a partition suit decreed on 30th March 1936, but in ignorance of this division the Income-tax Officer assessed the uncle to income-tax as manager of a joint family for 1936-37:

Held, that the assessment was valid with reference to Section 25A (3) of the Income-tax Act and having regard to Section 14 (1) of that Act the assessment could not be regarded as the assessment of the divided member's share of income.

* Under Section 3 (i) of the Madras Agriculturists' Relief Act (IV of 1938) " ' Person ' means an individual and includes an undivided Hindu family..... ; "

Under Section 3 (ii) proviso (A) " a person shall not be deemed to be an ' agriculturist ' if he has in either of the two financial years ending 31st March 1938, been assessed to income-tax under the Indian Income-tax Act, 1922, or under the income-tax laws of any Indian State, or foreign government."

Held further, *that under the Madras Agriculturists' Relief Act (IV of 1938), the family which had been assessed to income-tax notwithstanding its disruption, could not be deemed to be a person after 30th March, 1936, and the divided member was not disentitled to the benefits of the said Act.*

C. R. P. No. 1405 of 1942 (A. A. O. No. 110 of 1940, converted into C. R. P.)

Ch. Raghava Rao, for the petitioner.

B. V. Ramanarasu and *N. Vasudeva Rao*, for the respondents.

The Court delivered the following

JUDGMENT.

The petitioner was second defendant in a suit which was decreed against him and his uncle, the first defendant. He has been refused relief under Section 19 of Act IV of 1938 on the ground that he was not an agriculturist having been assessed to income-tax. In fact he became divided from his uncle as a result of a partition suit decreed on 30th March, 1936. In ignorance of this division the Income-tax Officer assessed the first defendant to income-tax as manager of a joint family for 1936-37. This assessment is valid with reference to Section 25A (3) of the Income-tax Act and having regard to Section 14 (1) of that Act the assessment cannot be regarded as the assessment of the second defendant's share of the income.

Under Act IV of 1938, the family which has been assessed to income-tax notwithstanding its disruption, cannot be deemed to be a person after 30th March, 1936. The petitioner is himself a person who has not in fact been assessed to income-tax and whose income could not be deemed to have been assessed by this assessment having regard to the provisions of Section 14 (1) of the Income-tax Act. We are therefore constrained to hold that the petitioner is not disentitled to the benefits of Act IV of 1938. We allow the revision petition with costs and direct that the decree be amended so as to make the petitioner liable for Rs. 2,500 with interest at 6 per cent. from 1st October, 1937, and costs Rs. 619-3-0 with interest thereon at 5 per cent. from 3rd April, 1935, to 22nd March, 1938, and thereafter at 6 per cent.

Petition allowed.

[IN THE BOMBAY HIGH COURT.]

GORDHANDAS T. MANGALDAS

v.

COMMISSIONER OF INCOME-TAX, BOMBAY.

BEAUMONT, C. J., and KANIA, J.

September 25, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922 AFTER AMENDMENT OF 1939),
 SEC. 25A—HINDU UNDIVIDED FAMILY—EXPRESS DECLARATION OF
 INTENTION TO PUT AN END TO JOINT STATUS—NO PHYSICAL DIVISION
 OF PROPERTY BY METES AND BOUNDS—ASSESSMENT—SCOPE OF
 SEC. 25A.

Where the members of a Mitakshara joint Hindu family consisting of a father and three sons and owning immovable properties put an end to their joint status by an express declaration of their intention to separate but the family property was not divided by metes and bounds:

Held, that the joint family property had not been partitioned in definite portions within the meaning of Section 25A (1) of the Indian Income-tax Act, 1922.

Section 25A contemplates a physical division of the joint family property; a mere division of interest in such property is not enough.

Saligram Ramlal v. Commissioner of Income-tax [1934] (2 I.T.R. 448) followed; Sher Singh Nathu Ram v. Commissioner of Income-tax [1934] (2 I.T.R. 479) dissented from.

Cases referred to :—

Biradhmah Lodha v. Commissioner of Income-tax (1934) 2 I.T.R. 164; I.L.R. 56 All. 504; 153 I.C. 722; A.I.R. 1934 All. 217; 1934 A.L.J. 1213.

Sir Bisesardas Daga, *In re* (1936) 4 I.T.R. 66; 9 I.T.C. 206.

Lachiram Baldeodas v. Commissioner of Income-tax, Bihar & Orissa (1936) 4 I.T.R. 279; 9 I.T.C. 471.

Saligram Ramlal v. Commissioner of Income-tax (1934) 2 I.T.R. 448; 7 I.T.C. 354; A.I.R. 1934 Lah. 942.

Sher Singh Nathu Ram v. Commissioner of Income-tax (1934) 2 I.T.R. 479; 8 I.T.C. 38; A.I.R. 1935 Lah. 81; 154 I.C. 191.

Sir Sundar Singh Majithia v. Commissioner of Income-tax, C. P. and U. P. (1942) 10 I.T.R. 457.

Case referred to the High Court of Bombay by the Income-tax Appellate Tribunal, Bombay Bench, under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by Section 92 of the Indian Income-tax (Amendment) Act, 1939 (VII of 1939), for decision of the following question of law:

“Whether on the facts of this case it has been rightly held that the joint family property of the petitioner and his sons has not been

partitioned in definite portions within the meaning of Section 25 A (1) of the Income-tax Act, 1922 ? ”

Income-tax Reference No. 6 of 1942 : The facts of the case appear in the Statement of Case and judgment of the Appellate Tribunal.

JUDGMENT OF APPELLATE TRIBUNAL.

Under Section 33 of the Indian Income-tax Act (XI of 1922), the Income-tax Appellate Tribunal, Bombay Bench, (consisting of N. R. Gundil, Judicial Member, and P. C. Malhotra, Accountant Member), delivered the following judgment on 28th November 1941.

“ This is an appeal from an order of the Appellate Assistant Commissioner of Income-tax, B Range, Bombay. It relates to the assessment made upon the appellant, Mr. Gordhandas T. Mangaldas, for the assessment year 1939-40. The Income-tax Officer computed the total assessable income at Rs. 44,647, but in appeal the Appellate Assistant Commissioner reduced it to Rs. 35,856. There is no further objection as to the amount of income assessed. And the only contest before us is in regard to the appellant being assessed on the income of the Hindu undivided family of which he is the father and manager.

2. Till the assessment year in question, the appellant and his three sons were a Hindu undivided family governed by the Mitakshara school of Hindu law, and the appellant used to be assessed on that footing in respect of the total family income which is chiefly derived from properties situated in Bombay. In the assessment of 1939-40 it was alleged that there was a partition in the family, the severance of coparcenary being expressed in several letters, dated 2nd and 3rd July, 1939, which the sons wrote to the father and to one another declaring their intention to separate and to enjoy their respective shares in the joint family property, stated to be one-fourth in each case in severalty. They also proposed to appoint Messrs. Little & Co., Solicitors, to act for them in the matter of completing the partition and preparing necessary Deeds of Settlement of their respective shares with a view to preserve them from being wasted. There is, however, no evidence on record that the appellant father gave a corresponding assent to his sons' declarations except claiming a partition before the Income-tax Officer and in appeal. But the matter appears to have been taken up by the Solicitors, although nothing further than preparing certain drafts of deeds was done till the date of the present assessment. There is no dispute as to these several facts. The learned Counsel expressly admitted before us that the family property has not been divided by metes and bounds.

3. In course of the assessment under consideration the appellant claimed a partition in the family on these facts, and asked the Income-tax

Officer to record an order under Section 25A (1) of the Act. The Officer made an enquiry and passed a separate order declining to record the partition. He held that no partition such as that contemplated by Section 25A (1) had taken place among the members of the family, inasmuch as the partition of the joint family property in definite portions had not been made. In appeal the learned Appellate Assistant Commissioner thought that a mere severance of the joint status implied in the several declarations of intention to separate did not suffice to bring the case within the purview of the section. While conceding that the section did not require an actual division of the joint family property by metes and bounds, the learned Appellate Assistant Commissioner thought at the same time that the section did demand a division of the property by an allotment of shares to different members; and that therefore in the absence of such a division the claim to an order under Section 25A (1) could not be accepted. From this decision the present appeal is taken; and the several grounds set out in the memorandum resolve into one main point whether there has been a partition of the undivided family property in definite portions so as to justify an order under Section 25A (1) of the Act.

4. But before proceeding to consider the main issue it will be well to dispose of a preliminary point taken by the learned Departmental Representative that the Tribunal has no power to entertain and decide the question of partition in this appeal. The facts bearing on the point may be very shortly stated. We have stated before that the claim to partition was made before the Income-tax Officer in course of the assessment. It was therefore in order. The Officer made the necessary enquiry and passed a separate order under Section 25A (1) on the same date as the assessment order. These orders were followed by a notice of demand under Section 29 of the Indian Income-tax Act. From the order-sheet it appears that no notice of two separate orders having been passed was served upon the appellant. He applied for a certified copy of the assessment order which was duly furnished to him. He then preferred an appeal to the Appellate Assistant Commissioner from the assessment contending, *inter alia*, that the Income-tax Officer was wrong in disallowing the claim to partition, without preferring a separate appeal from the order under Section 25A (1) which is provided by Section 30 of the Act. In these circumstances, the learned Departmental Representative contends that the Appellate Assistant Commissioner had no jurisdiction to entertain and decide the question of partition in a regular assessment appeal; and that consequently the Tribunal is precluded from entertaining the question either. Here it must be mentioned that the possibility of such a point

arising before the Appellate Assistant Commissioner seems to have been contemplated by the appellant who anticipated it in his memo of appeal below contending that he had not been furnished with a copy of the separate order under Section 25A; and that he came to know of it after he had received a copy of the assessment order in which the Income-tax Officer had made a reference to the latter. But the point as to the Appellate Commissioner's jurisdiction to consider the question of partition in a regular assessment appeal does not appear to have been raised before him, and, in consequence, the Officer probably thought that he had power to decide the question which had been expressly raised in the memorandum of appeal. In effect he treated the regular assessment appeal as one taken from an order under Section 25A also. We cannot say that the Appellate Assistant Commissioner acted without jurisdiction in these circumstances. There was also no question of loss of revenue, inasmuch as no fee is prescribed for an appeal before the Appellate Assistant Commissioner. At any rate, the appeal before us is specially to be taken on a point of partition, although it is registered as a regular assessment appeal, apparently because it had been so treated below. We therefore think that having regard to the peculiar circumstances above stated we ought not to take notice of a defect which appears to us to be too formal and throw out the appeal on the particular ground.

5. Coming to the main question, the substance of the learned Counsel's arguments is that in a joint Hindu family governed by the Mitakshara school an unequivocal expression of intention by a member or members constitutes a partition; and that, thereafter, they hold the joint family property in ascertained shares, an actual division by metes and bounds not being necessary to complete the severance. He contends further that holding of the family property in ascertained shares by the members is all that is required by Section 25A (1) of the Act, as amended in 1939. In other words, it is argued that an ascertainment of shares on a partition in the manner just stated amounts to a partition of the joint family property among the various members in definite portions contemplated by Section 25A, and that it is not necessary that there should be an actual division of the property by metes and bounds. There can be no doubt or dispute as to the correctness of these two propositions of Hindu law stated by the learned Counsel. At the same time, it must be borne in mind that such a kind of partition, *i.e.*, by an ascertainment of shares in the family property, primarily affects the questions of alienation and succession among Hindus with which we are not concerned in this case. The precise

point before us is whether a notional partition of family property by an ascertainment of the proportion of shares is all that is demanded by Section 25A (1) of the Income-tax Act which lays down that the Income-tax Officer shall record an order of partition if he is satisfied that the joint family property has been partitioned among the various members or groups of members in definite portions. In other words, the point we have to decide is whether an *ascertainment* of shares resulting from an unequivocal expression of intention to separate, *i.e.*, a notional division, amounts to a partition in *definite portions* within the meaning of the section. The learned Counsel's argument is that both the expressions mean the same thing, while it is contended on behalf of the Department that a mere notional ascertainment of shares does not suffice to fulfil the condition laid down by the section.

6. Judicial opinion on this important question presents a good deal of divergence. Each side has cited decided authorities in support of its contention, and we shall notice several.....that appear to be more important than the rest. Here it may be pointed out that all these cases were decided under Section 25A before its amendment in 1939. As it then stood, the section required an Income-tax Officer to satisfy himself first that a separation of the members of a Hindu family had taken place, and secondly, that the joint family property had been partitioned among the various members in definite portions. The amendment of 1939 deleted the first of these two requirements and retained the second. So that assistance of these several cases may yet be sought as to the meaning of the second condition retained in the section. In *Biradhmaj Lodha v. Commissioner of Income-tax, U. P.*¹ Niamatullah, J., held that Section 25A (1) contemplates a case in which a disruption of a Hindu family occurs, so that a joint family ceases to exist and no property previously belonging to it retains the character of a joint family property; and that, therefore, it is immaterial whether the property is divided by metes and bounds or is held in defined shares. His Lordship thought that a partition contemplated by Section 25A (1) is not necessarily a partition by metes and bounds: *vide* page 178 of the report. But with the greatest respect to his Lordship we cannot help thinking that his observations went much further than the answer that the question raised in that case required. For it will be clear from page 165 of the report that the precise question before their Lordships was whether in the case of a partial division of a joint family property Section 25A has any application. It was not a case of complete partition of the family property. Also the family had

retained its joint status. And, consequently, Bennet, J., who was a party to the decision answered that a division of a particular portion of the joint family property did not fulfil the requirements of Section 25A (1). Thus the observations of Niamatullah, J., appear to be more or less *obiter dicta*. *Biradhma's case*¹ was decided on November 3, 1933. On July 22, 1934, the question, as it arises in this case, directly arose before a Division Bench of the Lahore High Court in *Saligram Ramlal v. Commissioner of Income-tax, Punjab*², and their Lordships held that Section 25A of the Income-tax Act contemplates an actual partition by metes and bounds of the joint family property and not a mere change of coparcenary to a tenancy-in-common by a severance of the joint status. *Biradhma's case*³ was neither cited at the bar nor noticed in their Lordships' judgment. The question once again came up before a Full Bench of the same High Court on October 19, 1934, in *Sher Singh Nathu Ram v. Commissioner of Income-tax, Punjab*⁴. Dalip Singh, J., who delivered the judgment of the Full Bench thought that a partition by metes and bounds was not necessary to bring a case under Section 25A (1). His Lordship observed that the word "share" was synonymous for "portion", so that the expression partition in "definite portions" means the same thing as partition in "definite shares." This case was followed by the Judicial Commissioner's Court, Nagpur, in *Sir Bisesardas Daga and Others, In re*⁵ on January 7, 1935, in which reference is made to *Biradhma Lodha's case*⁶ also. Lastly, the most recent case cited before us by the learned Departmental Representative is that of *Lachiram Baldeodas v. Commissioner of Income-tax, Bihar and Orissa*⁷, decided by the Patna High Court on May 7, 1936. In this case too, a reference to the several cases noticed above is not found. Wort, C. J., held that under Section 25A the Income-tax Officer was not concerned with a notional separation of the family and that he has to enquire into the question whether the joint family property has *in fact* been divided. It appears to us from his judgment that his Lordship made a distinction between partition by a notional ascertainment of shares and a division of the property *in fact*.

7. Thus the question raised before us presents considerable difficulty in view of the conflict of opinion among the different High Courts and also different Benches of the same High Court, as well as in the absence of a Bombay decision which would be binding upon us in Bombay. We are therefore left to give our own answer on a careful consideration of the several judgments read with the provisions of

(1) (1934) 2 I.T.R. 164.

(2) (1934) 2 I.T.R. 448.

(3) (1934) 2 I.T.R. 479.

(4) (1936) 4 I.T.R. 66.

(5) (1936) 4 I.T.R. 279.

Section 25A of the Indian Income-tax Act. We have stated before that the question raised in *Biradhmal Lodha's case*¹ was materially different, being one of a partial partition. In the rest of the cases, however, the question that is now raised before us was specifically referred for decision. We have to observe that the Income-tax Act provides for assessment of Hindu families after partition, that is to say, if the co-owners desire to be assessed as separate units they must own incomes which can be regarded as separate entities. It is extremely difficult to say that the income of a share notionally separated on an ascertainment merely by the severance of status can at all be regarded as a separate entity for the purposes of the tax. In the Lahore Full Bench case *Dalip Singh, J.*, observed that the word "portion" used in the section is identical in meaning with "share"; and, in this connection, his Lordship referred to their dictionary meaning. But with the greatest respect to his Lordship it must be said that the words "portion" and "share" carry somewhat different meanings in ordinary language in the light of which we have to construe the former word occurring in the Income-tax Act. We do not generally speak of a notional share as a portion. For instance, we speak of a portion of a house to let, and not a share. The word "partition" in its ordinary sense would mean a division of property between co-owners, and not a mere conversion of coparcenary into a tenancy-in-common. Although we do not intend to go as far as to say that there must be a division by metes and bounds of family property before a Hindu assessee can claim an order under Section 25A, we respectfully agree with the dictum of Wort, C. J., in *Lachiram Baldeoas v. Commissioner of Income-tax, Bihar and Orissa*², that a division in fact is necessary under Section 25A (1). Such a division will be sufficiently made by an allotment of shares among the members of the family and not merely by a notional ascertainment of their proportions in relation to the whole. That is what we think Wort, C. J., meant by a division *in fact*. This view, in our opinion, is supported by the language of Section 25A (2) which provides for separate assessment of a divided member of a Hindu family. The concluding portion of the sub-section is to the effect that a divided member shall be liable for a share of the tax on the income so assessed (*i.e.*, assessed on the total income of the family) according to the portion of the joint family property *allotted* to him. We therefore think that there must at least be an allotment of a share to a member of the family before he can claim to be assessed as a separate unit. That is not so in the present case. Lastly, one cannot overlook that Section 25A of the Income-tax Act provides machinery

(1) (1934) 2 I.T.R. 164.

(2) (1936) 4 I.T.R. 279.

for making separate assessments of divided members of a Hindu family, and we are afraid that construing Section 25A (1) in the manner urged on behalf of the appellant would make the provisions unworkable, since such a construction would conflict with the language of the concluding portion of Section 25A (2) which we have just noticed. In conclusion we desire to add that controversy like the present which is bound to arise in future also would be set at rest by amending Section 25A (1) to fall in line with sub-section (2) of that Section as indicated above.

8. For these reasons we hold that the appeal must fail on the main point arising in this case. We therefore confirm the Appellate Assistant Commissioner's order and dismiss this appeal."

On the application of the assessee under Section 66 (1) of the Indian Income-tax Act (XI of 1922) the Appellate Tribunal referred the case to the Bombay High Court.

STATEMENT OF CASE.

" This is an application under Section 66 (1) of the Indian Income-tax (Amendment) Act, 1922, asking us to refer certain questions of law stated to arise out of our appellate judgment in Regular Assessment Appeal No. 44, Bombay, of 1941-42. The petition is marked Ex. A, in the appended list.

2. The Commissioner of Income-tax, Bombay, Sind and Baluchistan, has filed a written answer, Ex. B, in which it is conceded that our judgment does give rise to a question of law.

3. In paragraph 5 of his petition, the petitioner has formulated three questions. But we agree with the Commissioner in thinking that the first two involve only one point, and that the third is unnecessary.

4. The undisputed facts of this case have been sufficiently set out in paragraphs 2 and 3 of our appellate judgment a copy of which is marked Ex. C.* We propose to re-state them very briefly. The petitioner and his three sons formed a Hindu undivided family till July 3, 1939, when they put an end to their joint status by express declarations of their intention to separate. Nothing further was done to divide the family property, although it was proposed to appoint Messrs. Little & Co., for completing the partition and preparing the necessary Deeds of Settlement. That was the position during the proceedings of assessment for the charge year 1939-40. In course of these proceedings the petitioner, Mr. Gordhandas, made an application, dated July 17, 1939, requesting the Income-tax Officer to record an order of partition under Section 25A (1), so that separate assessments might be made upon the individual members in respect of their shares

* Printed *supra* at p. 184.

of the family income under Section 25A (2) of the Act. After making the necessary enquiry the Income-tax Officer passed an order, dated February 1, 1941, holding that no partition had taken place in the family, and that the joint family property had not been partitioned among the various members in definite portions. A copy of the order is Ex. D.

5. The petitioner appealed to the Appellate Assistant Commissioner who held that a severance in intention had been effected among the different members of the family by the declarations contained in the several letters. At the same time he thought that such a severance in intention did not suffice to bring the case within the purview of Section 25A (1) the provisions of which, in his opinion, required that a division of property by allotment of shares to different members should be proved before an order under that section could be made. He therefore, dismissed the appeal. A copy of his order is marked Ex. E.

6. The petitioner took the order in appeal to the Appellate Tribunal in Regular Assessment Appeal No. 44, Bombay, of 1941-42. After hearing the appellant's counsel and the Departmental Representative, we confirmed the Appellate Assistant Commissioner's order and dismissed the appeal. In substance, our finding was that a mere severance of status by means of an express intention to separate and a consequent notional ascertainment of the proportions of the shares of the different members, did not suffice to answer the requirements of Section 25A (1) of the Indian Income-tax Act, and that there must be a partition of the family property in definite portions by an allotment of shares to the different members before an order under that section could be made.

7. At this point we cannot help bringing to their Lordships' notice an inaccurate statement contained in paragraph 4A (2) of the present petition to the effect that we committed an error of law in holding that the consent of the father was necessary to effect the partition of the joint family. We have not recorded any such finding at all. In paragraph 2 of our judgment while stating the facts, we made an observation that there was no evidence of a specific declaration of intention by the father to effect a severance. But that was only a casual remark, for, at the same time we substantially held that the application which the petitioner made to the Income-tax Officer could spell out such an intention on his part. As a matter of fact, we proceeded upon the common ground that a severance of status had been effected among the petitioner and his three sons, and applied ourselves more particularly to the question whether such a severance and a notional ascertainment

of shares of the different members brought the case within the purview of Section 25A (1) of the Act.

8. Section 25A (1) lays down that where, at the time of making an assessment under Section 23, it is claimed by or on behalf of any member of a Hindu family hitherto assessed as undivided that a partition has taken place among the members of such family, the Income-tax Officer shall make such inquiry thereinto, as he may think fit, and, if he is satisfied that the joint family property has been partitioned among the various members or groups of members in definite portions, he shall record an order to that effect. Sub-section (2) of that section describes the manner in which separate assessments may be made upon the divided members of a Hindu family consequent upon an order under Section 25A (1). Each of such members becomes liable for a share of the tax on the income assessed according to the portion of the joint family property *allotted* to him.

9. It will be seen from the concluding portion of paragraph 5 of our judgment that the question that we set for decision was whether an ascertainment of the proportion of shares resulting from an expression of unequivocal intention to separate, *i.e.*, a notional division, amounts to a partition in definite portions within the meaning, and for the purposes, of Section 25A (1) of the Income-tax Act.

10. The point presented a good deal of difficulty in view of divergence of judicial opinion. We made a detailed review of the several cases cited before us in paragraphs 6 and 7 of our judgment, and finally came to the conclusion that a mere severance of status and a notional partition by ascertainment of the proportions of different shares in relation to the whole of the joint family property fell short of the requirements of Section 25A (1) of the Act, and that there must be at least an allotment of shares to different members of the family before they can claim to be assessed as separate entities. In the present case we held, as was also admitted, that there was no actual division of the family properties nor even an allotment of shares.

11. Therefore, the only question of law that arises on this reference which we respectfully submit to their Lordships is:—

Question referred.—"Whether on the facts of this case it has been rightly held that the joint family property of the petitioner and his sons has not been partitioned in definite portions within the meaning of Section 25A (1) of the Indian Income-tax (Amendment)* Act. 1922?"

V. E. Taraporewala with *M. M. Jhaveri*, for the assessee.
M. C. Setalvad, for the Commissioner.

The word (Amendment) has been inserted here through oversight.—Ed.

JUDGMENT.

BEAUMONT, C. J.—This is a reference made by the Appellate Tribunal, Bombay Bench, under Section 66 (1) of the Indian Income-tax Act, raising a question which has given rise to a difference of judicial opinion. The question is :

“Whether on the facts of this case it has been rightly held that the joint family property of the petitioner and his sons has not been partitioned in definite portions within the meaning of Section 25A (1) of the Indian Income-tax (Amendment) Act, 1922 ?”

The facts giving rise to the question have never been in dispute. The assessment year is the year 1939-40, and down to July 3, 1939, there was a Hindu joint family consisting of the father and three sons, and on that date severance took place. The three sons all intimated an unequivocal desire to sever the joint family, and according to the law applicable to Hindu joint families under the Mitakshara system that expression of a wish on the part of the sons severed the joint family, and, as there were only four coparceners, the necessary result was that the shares in the joint family property became divided equally between the four coparceners, who then held as tenants-in-common. But there has been no physical division of the joint family property. I use the expression “physical division” in preference to the more usual expression “division by metes and bounds,” because the latter expression is only applicable strictly to immovable property. Both the Assistant Commissioner and the Appellate Tribunal considered that a mere severance of the joint family was not enough for the purpose of Section 25A: that there must be an allotment of shares, though both Tribunals thought that a physical division was not necessary. I must confess that I do not follow that opinion. It appears to me perfectly plain, on the finding that the joint family severed in July, 1939, that the shares were definitely ascertained, and there being four members of the family each became entitled to a one-fourth share of the family property. To my mind, the real question to be determined is whether Section 25A requires a physical division, or is satisfied only by a division in interest.

Before coming to Section 25A, it is to be noticed that a joint Hindu family is one of the taxable units under Section 3 of the Indian Income-tax Act, and that Section 14 (1) provides that the tax shall not be payable by an assessee in respect of any sum which he receives as a member of a Hindu undivided family. That, of course, is designed to avoid double assessment. If the family pays, the individual members are not required to pay.

Section 25A (1) before the amendment of 1939 provided :

“ Where, at the time of making an assessment under Section 23, it is claimed by or on behalf of any member of a Hindu family hitherto assessed as undivided that a partition has taken place among the members of such family, the Income-tax Officer shall make such inquiry thereinto as he may think fit, and, if he is satisfied that a separation of the members of the family has taken place and that the joint family property has been partitioned among the various members or groups of members in definite portions.....he shall record an order to that effect.”

Sub-section (2) deals with assessment when an order is made under sub-section (1), and under sub-section (3) the family is to be deemed to be undivided unless an order is passed under sub-section (1).

In this case we are dealing with the section as amended in 1939, and in the amended sub-section (1) the words “ that a separation of the members of the family has taken place and ” are omitted, so that the Income-tax Officer instead of having to be satisfied of two things, that a separation of the members of the family has taken place and that the joint family property has been partitioned, is now only required to be satisfied of one thing, namely, that the joint family property has been partitioned among the various members or groups of members in definite portions.

The question arising is whether the requirement that the Income-tax Officer shall be satisfied that the joint family property has been partitioned among the various members in definite portions, requires him to be satisfied that the property has been physically divided, or merely that there has been a division in interest.

In construing the Act we have to remember that it is an all-India Act, and that it is as applicable to Hindu families under the Dayabhaga system, as to those under the Mitakshara system. Under the Mitakshara system there are always two steps in a complete partition. There is, first, the division in interest, which may be brought about by agreement, by filing a suit, or by expressing an intention to divide, and there is the physical division of the property, which may, and often does, take place, years after the division in interest. But under the Dayabhaga system the members of the joint family are divided in interest; they are in a position analogous to that of tenants-in-common, that is to say, they are originally in much the same position as the members of a Mitakshara family after the family has disrupted, and there has been a division in interest. I do not see what effect Section 25A can have on the property of a Dayabhaga joint family, if the opinion of the Income-tax Officer must be directed merely to a division

in interest which always existed. It seems to me that Section 25A will have no effect at all on families under the Dayabhaga system, unless it is held to involve a physical division into definite portions.

Sub-section (2) of the section also seems to me to favour that construction of the first sub-section, because it provides that where an order has been passed under sub-section (1), the Income-tax Officer shall make an assessment of the total income received by or on behalf of the joint family as such, as if no separation or partition had taken place, and each member or group of members shall, in addition to any income-tax for which he or it may be separately liable, and notwithstanding anything contained in sub-section (1) of Section 14, be liable for a share of the tax on the income so assessed according to the portion of the joint family property allotted to him or it. It is argued by the assessee that "according to the portion of the joint family property" means according to the proportion or share of the joint family property. But Mr. Setalvad on behalf of the Commissioner contends that the word "portion" is used in exactly the same sense as in sub-section (1), and refers to a physical part of the property; he suggests, I think correctly, that sub-section (2) is designed, at any rate in part, to meet the case in which there has been a partition of joint family property, where one member gets a portion producing income, and another member gets a portion producing less income, or no income at all, for instance, where one member of the joint family takes income producing lands or shares, and another member takes jewellery of considerable capital value, but producing no income. It would be unfair in such a case to apportion the income amongst the members in proportion to the value of the shares they take. The allocation of the tax ought to be made in accordance with the particular portion of the property which each member has taken.

Apart from authority, I should feel no doubt that Section 25A contemplates a physical division of the property. I think that the expression "definite portions" indicates a physical division in which a member takes a particular house in which he can go and live, or a piece of land which he can cultivate, or which he can sell or mortgage, or takes particular ornaments which he can wear or dispose of, and that the expression "definite portions" is not appropriate to describe an undivided share in property where all a particular member can claim is a proportion of the income, and a division of the corpus, but where he cannot claim any definite portion of the property. In a case in the Lahore High Court, to which I will refer more in detail later, the bench suggested, in construing Section 25A, that the words "portion" and "share" were synonymous. But that, I think, is not so. No

doubt, the words sometimes may be used interchangeably, but in connection with property I should say that a portion means a part of the property, whereas a share indicates the interest of some individual in the property. A room may be said to be a portion of a house; it cannot be said to be a share of a house, although it may represent the share of a particular person in the house. "Portion" seems to me the apt word for division of property, and "share" for division of interest, and it is significant that "portion" is used in Section 25A. No doubt the expression "division in definite portions" will have to be construed with regard to the nature of the property concerned. A business cannot be divided into parts in the same manner as a piece of land; division may only be possible in the books. Special cases will have to be dealt with by the Income-tax Officer when they arise. If he comes to the conclusion that, having regard to the nature of the property, what has been done amounts to a division in definite portions, he will record his finding under sub-section (1); if he comes to the conclusion that it does not, then he will have to go on assessing the family under sub-section (3).

The cases on this subject are conflicting, as the Tribunal has noticed. In the first place, there are two decisions of the Lahore High Court, which are in conflict. The first one, decided on June 22, 1934, by Mr. Justice Addison and Mr. Justice Sale is *Saligram Ramlal v. Commissioner of Income-tax*¹, and the bench held that Section 25A of the Indian Income-tax Act contemplates an actual partition by metes and bounds of the joint family property and not a mere change of the coparcenary to a tenancy-in-common by a severance of the joint status. The second case in the Lahore High Court, decided by three Judges, Mr. Justice Jai Lal, Mr. Justice Dalip Singh and Mr. Justice Skemp, on October 19, 1934, is *Sher Singh Nathu Ram v. Commissioner of Income-tax*², and that bench arrived at a precisely opposite conclusion, without any reference to the earlier decision, which presumably was not brought to their attention. The leading judgment which was delivered by Mr. Justice Dalip Singh treats the words "share" and "portion" as synonymous, and reads Section 25A as requiring only partition in definite shares. As I have already said, I do not agree with that view. Moreover, with all deference to the bench, I think they fell into an error in saying that there are three stages in the partition of a Hindu family subject to the Mitakshara law; the first stage being a disruption without ascertainment of shares, the second, disruption of family with ascertainment of shares, and, the third, a division of property. I do not think it is correct to say that there are more than two stages: a division in interest, and a physical division of the property. Directly

(1) (1934) 2 I.T.R. 448; 7 I.T.C. 354.

(2) (1934) 2 I.T.R. 479; 8 I.T.C. 38.

there is a disruption of the family, that necessarily determines that the shares belong in severalty to the members of the family according to law. Of course, in every case of partition, before a final division takes place, three things must be determined: the property to be divided; the shares into which it is to be divided; and the persons entitled to those shares. In uncontested cases these matters are settled by agreement; in contested cases they may have to be determined by the Court. But their determination is part of the machinery for effecting the final partition, and does not form an independent stage in partition. In my opinion, the judgment of the earlier bench of the Lahore High Court is to be preferred to that of the later bench.

Then there is a decision of a bench of the Allahabad High Court in *Biradhmāl Lodha v. Commissioner of Income-tax*¹ in which it was determined only that Section 25A did not apply to a partial division of joint family property, a view recently accepted by the Privy Council. That question is not before us, but Mr. Justice Niamatullah, in the course of his judgment, said that a division by metes and bounds was not required for the purposes of Section 25A. The question did not really arise in that case and moreover the property in question was a business, to which as I have already suggested, special considerations may apply. In my opinion, that case is no authority on the question we have to determine on the construction of Section 25A.

Then there is a decision of the Judicial Commissioner's Court at Nagpur, *Sir Bisesardas Daga, In re*², in which the Court said that they followed the view of the Allahabad High Court in the case which I have just mentioned, and considered that Section 25A did not demand partition by metes and bounds. There, again, they were dealing with a business, and they were also influenced by the fact that the Commissioner admitted that a division by metes and bounds was not necessary.

Then there is a decision of the Patna High Court in *Lachiram Baldeodas v. Commissioner of Income-tax, Bihar*³. The Acting Chief Justice in that case expressed the opinion that Section 25A contemplated physical division of the property, but I think that was no more than a dictum.

Then there is a very recent decision of the Privy Council in *Sir Sundar Singh Majithia v. Commissioner of Income-tax, U.P. and C.P.* which has not yet been reported⁴. In that case this question did not definitely arise, but on one aspect of the case the Board held that it was necessary to consider the effect of Section 25A and the judgment contains observations on the section which are of considerable assistance

(1) (1934) 2 I.T.R. 164; I.L.R. 56 All. 504.

(2) (1936) 4 I.T.R. 66; 9 I.T.C. 206.

(3) (1936) 4 I.T.R. 279; 9 I.T.C. 471.

(4) Since reported as (1942) 10 I.T.R. 457.

in the present case. Their Lordships point out that Section 25A is directed to the difficulty which arose when an undivided family had received income in the year of account but was no longer in existence as such at the time of assessment, and they point out that the provision of Section 14 (1) must be borne in mind in considering the terms of Section 25A. Then their Lordships go on :—

“Section 25A deals with the difficulty in two ways, which are explained by the rule applicable to families governed by the Mitakshara, that by a mere claim of partition a division of interest may be effected among coparceners so as to disrupt the family and put an end to all right of succession by survivorship. It is trite law that the filing of a suit for partition may have this effect though it may take years before the shares of the various parties are determined or partition made by metes and bounds. Meanwhile the family property will belong to the members as it does in a Dayabhaga family—in effect as tenants-in-common. Section 25A provides that if it be found that the family property has been partitioned in definite portions, assessment may be made, notwithstanding Section 14 (1), on each individual or group in respect of his or its share of the profits made by the undivided family, while holding all the members jointly and severally liable for the total tax. If, however, though the joint Hindu family has come to an end, it be found that its property has not been partitioned in definite portions, then the family is to be deemed to continue—that is to be an existent Hindu family upon which assessment can be made on its gains of the previous year.”

The Board do not say in express words what they mean by the words quoted “partitioned in definite portions,” as no question as to their interpretation arose but it seems to me that the Board contemplated a physical division of the property, because the passage quoted shows that they had distinctly in mind the Dayabhaga system, under which no division in interest is necessary.

In my opinion, on the words of Section 25A of the Indian Income-tax Act we ought to answer the question put to us in the affirmative, because there has been no physical division of the joint family property. The authorities in India are conflicting, and as I read the decision of the Privy Council, although it is not directly in point, it favours the view that a physical division of the property is required.

The assessee to pay costs.

KANIA, J.—The relevant facts, sections of the Income-tax Act and authorities cited at the bar have been referred to in the judgment just delivered by the learned Chief Justice.

The question for consideration is whether on the construction of Section 25A in addition to the unequivocal declaration or decision of a member of a joint Hindu family to disrupt the joint status, in order that individual members may be assessed in respect of the property coming to their share, is it necessary further to show that the joint family property has been partitioned amongst the members in definite portions? It is material to bear in mind the scheme of the Income-tax Act, in the first instance. Under Sections 2 and 3 the different units stated therein are liable to be taxed as such. One of them is a joint Hindu family. In order to avoid double taxation, Section 14 lays down that when the individual member is being assessed, his income as a member of a joint family should not be assessed again. Then comes the stage, what happens when a family, which has once been so assessed, comes to a partition. To meet that contingency, Section 25A has been enacted. In the section, as it existed before the amendment of 1939, in terms the Income-tax Officer required proof, (i) that a separation of the members of the joint family had taken place and (ii) that the joint family property had been partitioned amongst the various members or groups of members in definite portions. On being satisfied on those points he had to record an order to that effect. The effect of such a recording was that the joint family income would be assessed and recovered in terms of sub-section (2). In the absence of such order, under sub-section (3) the joint family continued to be assessed as before.

The question before the Court is whether in respect of a Mitakshara family, if it is only shown that the joint family status has ceased to exist, the case is governed by Section 25A (1). In the present case the record shows that the applicant's joint family owns immovable properties, and it is not suggested that there is any business. The record further shows that there has been an agreement amongst the members and the joint family has ceased to exist. It is further shown that Messrs. Little & Co. were instructed to prepare the relative documents to divide the properties amongst the parties according to their shares, and drafts were prepared but that nothing more had been done up to the relevant time.

The argument on behalf of the applicant is that under Section 25A, once the joint family status had come to an end, the shares were ascertained, and the latter part of the section must mean that the joint family property had been partitioned in definite portions. In the first instance, it may be noted that the word "portion," when read in conjunction with partition of joint family property, would ordinarily mean a physical division, and not a definition or ascertainment of shares only. It was argued that under the Hindu law on an unequivocal expression of

intention to sever, the joint family status came to an end, and the Income-tax law could not be framed to alter that substantive law. I think this argument is fallacious, because by the Income-tax Act no attempt is made to alter the substantive law. The Income-tax Act only lays down the manner in which the income of what was once a joint family estate should when it is alleged that the joint family had come to a partition, be assessed. The scheme is that if it is proved to the satisfaction of the Income-tax Officer that there was not only a rupture of the joint family status, but definite portions of the joint family property, according to the words used in sub-section (2), had been allotted to individual members, those members were to be assessed in respect of the income allotted to their share.

If the omission of the words in the old section is to be used in construing the new one, it seems to me that the same favours the view urged by the Commissioner rather than of the applicant. In the amended section the words "a separation of the members of the family has taken place" have been omitted. That means that out of the two facts for which proof had to be furnished to the Income-tax Officer, proof of the first had become unnecessary. The question is why? And the answer obviously is that it is immaterial if the second is proved. If the applicant's contention was sound, the second part of the old sub-section should have been omitted and not the first, because in that event, once it was established that the joint family status has ceased to exist, no further proof was required. The retention of the second portion, and the omission of the first, in my opinion, emphasize the view that a division, that is a physical partition of joint family property in definite portions, is required to be proved.

In this connection it is material to bear in mind the Hindu law of joint family. It should be noted that Section 25A is of all-India application, and applies equally to joint families governed by the Mitakshara law and the Dayabhaga law. According to the Dayabhaga law, as stated in all recognised text-books, the members of a joint family have always a definite and ascertained share, that is a share which is not liable to be increased or decreased by the death or birth of another member in the family. Bearing that important distinction between the Dayabhaga law and the Mitakshara law in mind, if Section 25A is approached, it is clear that the last part of the section must mean a physical division on partition, because the separate ascertained shares amongst the members of a joint Hindu family governed by the Dayabhaga law already exist before any partition. This point of view is very clearly brought out in the very recent, but up to now unreported, judgment of the Privy Council, out of which the learned Chief Justice has quoted *in*

*extenso*¹. That passage clearly shows the interpretation put by their Lordships on Section 25A of the Income-tax Act as affecting the assessment of joint families governed by the Mitakshara law. Their Lordships in the first portion say that "by a mere claim of partition a division of interest may be effected among coparceners so as to disrupt the family and put an end to all rights of succession by survivorship." Then they further state that on such a declaration the effect is that the family property will belong to the members *as it does in a Dayabhaga family—in effect as tenants-in-common*. The result, therefore, is that their Lordships emphasize the view that on the declaration made by a member to sever his tie with the family, the result is what would be the normal state of affairs in a joint family governed by the Dayabhaga law. The passage quoted in the judgment then goes on to state that Section 25A provides that if it be found that the family property has been partitioned in definite portions, assessment may be made on each individual in respect of his share of the profits. But the concluding words emphasize clearly that if such division is not made, the joint family will continue to be assessed as a unit, as it had been assessed before. That passage clearly shows that although the first stage, namely, the declaration of a member to disrupt the family, may be effective, unless the second stage, namely, the division of the property amongst members in definite portions is also shown, the family will be continued to be assessed as a joint family unit.

Five decisions of Indian Courts, which have been referred to in the judgment of the learned Chief Justice, were cited at the bar. In all of them the question was in respect of what was once a joint family business. In most of them the question was whether, after the members severed one portion of the joint family asset and entered into a partnership agreement in respect thereof, the Income-tax Officer should have recorded the partnership agreement under Section 26A, or whether such an agreement amounted to a severance of that asset from the rest of the joint family property. Directly none of those cases had to deal with what was to be done unequivocally under Section 25A, in order that individual members may claim to be assessed separately. The observations in those cases have to be read along with the facts, and I emphasize this particularly in respect of the observations of Mr. Justice Niamatullah in *Biradhmāl Lodha v. Commissioner of Income-tax*². The learned Judge there stated that it was not necessary to have a division by metes and bounds, but it should be remembered that, correctly speaking, it is not possible to

(1) Since reported in *Sir Sundar Singh Majithia v. Commissioner of Income-tax, C.P. and U.P.* (1942) 10 I.T.R. 457.

(2) (1934) 2 I.T.R. 164, 177.

have a division by metes and bounds of a business, except by winding it up and rebringing the assets under a new partnership agreement. The view of Mr. Justice Dalip Singh in *Sher Singh Nathu Ram v. Commissioner of Income-tax*¹ appears to be somewhat widely expressed, and it must be recognized that the word "portion" is not necessarily under all circumstances interchangeable with the word "share." The question is always, having regard to the context in each case, what is the proper meaning to be attached to the word "portion." With respect, I differ from the conclusion of the bench of the Lahore High Court which decided the case of *Sher Singh Nathu Ram v. Commissioner of Income-tax*¹ where they held that "portion" and "share" were synonyms for the purpose of Section 25A (1). The other cases cited at the bar had dealt with the question of business, and in no case this particular view, namely, what was to be done for bringing the case under Section 25A, when the joint family estate consisted of immovable properties, had been independently considered. All the observations and discussions are in respect of a business which was contended to have been separately carried on after a particular date by members under an alleged agreement of partnership. In my opinion those cases do not directly bear on the point. As has been pointed out *Saligram Ramlal v. Commissioner of Income-tax*² is the only decision in which this question was distinctly dealt with, and the view there expressed is in consonance with the view expressed in this judgment.

I, therefore, agree that the question should be answered as stated in the judgment of the learned Chief Justice.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

MAHARAJA OF PATIALA

v.

COMMISSIONER OF INCOME-TAX (CENTRAL), BOMBAY.

BEAUMONT, C.J., and KANIA, J.

September 24, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE AMENDMENT OF 1939),
SECS. 4, 22 (2), 24B, 34, 38, 42, 43, 66—NON-RESIDENT—ASSESSMENT
WITHOUT APPOINTING AGENT—LEGALITY—RE-ASSESSMENT—NOTICE
UNDER SEC. 22 (2) SERVED AFTER ONE YEAR—WHETHER CAN BE
TREATED AS NOTICE UNDER SEC. 34—NOTICE SERVED ON LEGAL

(1) (1934) 2 I.T.R. 479,

(2) (1934) 2 I.T.R. 448.

REPRESENTATIVE—SUBMISSION OF RETURN BY AGENT AND ASSESSMENT ON DECEASED PERSON—VALIDITY OF NOTICE AND ASSESSMENT—REFERENCE—NEGATIVE QUESTIONS.

Under Section 42 of the Income-tax Act, 1922, before its amendment in 1939, a non-resident foreigner could be assessed without appointing an agent under Section 43.

A notice issued under Section 22 (2) read with Section 24B must make it clear that it is served on the person as the legal representative of the deceased and that the return required is that of the deceased's income.

When a notice is given in terms under Section 22 (2), which subsequently turns out to be a bad notice under that section because it is out of time, it cannot be held automatically to be a good notice under Section 34 when there is no reason for supposing that the Income-tax Officer ever considered the question under Section 34.

The late Maharaja of Patiala who had income from property and business in British India died on March 23, 1938. On November 23, 1938, the Income-tax Officer, Bombay, sent two printed notices under Sections 22 (2) and 38 of the Income-tax Act addressed to the Maharaja of Patiala requiring him to make a return of his income from all sources for the assessment years 1937-38 and 1938-39. The returns were signed by the Foreign Minister and were sent to Bombay. The Income-tax Officer subsequently passed the assessment orders and against the assessee in both the orders was written "His Highness.....late Maharaja of Patiala." It was contended on behalf of the Maharaja that the notices and assessments were invalid :

Held, (i) that the notice of the year 1937-38 not having been served until November 1938, was barred by time, and it could not be treated as a notice under Section 34 ;

(ii) that it is wholly irregular to assess a deceased person and the assessment should have been made on the legal representative in respect of the income of the deceased. But as the present Maharaja was the legal representative of the late Maharaja and as the return of the late Maharaja's income was made by the Foreign Minister on behalf of the Maharaja who knew perfectly well that what was being assessed was the income of his predecessor, the assessment, though not strictly made in accordance with the provisions of Section 24B, was in the circumstances valid.

BRAUMONT, C. J.—*It is not necessary that a notice under Section 34 should assume any particular form, but it must give notice to the assessee that in the opinion of the Income-tax Officer some income has escaped assessment.*

Practice of the Income-tax Appellate Tribunal of stating questions in the negative for the decision of the High Court condemned.

Maharaja of Benares v. Commissioner of Income-tax [1938] (6 I.T.R. 217) dissented from.

Tischler & Co. v. Apthorpe [1885] (2 Tax Cas. 89); Werle & Co. v. Colquhoun [1888] (2 Tax Cas. 402); Whitney v. Inland Revenue Commissioners [1925] (10 Tax Cas. 88); [1926] A.C. 37); Chief Commissioner of Income-tax v. Bhanjee Ramjee and Co. [1921] (44 Mad. 773); Commissioner of Income-tax, Bombay v. National Mutual Association of Australasia Ltd. [1933] (57 Bom 519; 1 I.T.R. 350) and Commissioner of Income-tax, Bengal v. Mahaliram Ramjidas [1940] (8 I.T.R. 442; 67 I.A. 239) followed.

Cases referred to :—

Chief Commissioner of Income-tax, Bengal v. Bhanjee Ramjee and Co. (1921) 44 Mad. 773; 1 I.T.C. 147.

Commissioner of Income-tax, Bengal v. Mahaliram Ramjidas (1940) 67 I.A. 239; 42 Bom. L.R. 997; 8 I.T.R. 442; 44 C.W.N. 929; A.I.R. 1940 P.C. 124.

Commissioner of Income-tax, Bombay v. National Mutual Association Australasia Ltd. (1933) 57 Bom. 519; 35 Bom. L.R. 896; A.I.R. 1933 Bom. 427; 1 I.T.R. 350; 6 I.T.C. 426.

Jawala Prasad v. Commissioner of Income-tax (1935) 3 I.T.R. 295.

Maharaja of Benares v. Commissioner of Income-tax (1938) 6 I.T.R. 217; 1938 All. 432; 176 I.C. 167; 1938 A.L.J. 341; A.I.R. 1938 All. 310.

Rogers Pratt Shellac & Co. v. Secretary or State for India (1924) 52 Cal. 1; 83 I.C. 273; 28 C.W.N. 1074; A.I.R. 1925 Cal. 34; 1 I.T.C. 363.

Tischler & Co. v. Apthorpe (1885) 52 L.T. 814; 2 Tax Cas. 89.

Werle & Co. v. Colquhoun (1888) 20 Q.B.D. 753; 57 L.J.Q.B. 323; 58 L.T. 756; 36 W.R. 613; 2 Tax Cas. 402.

Whitney v. Inland Revenue Commissioners (1926) 95 L.J.K.B. 165; 134 L.T. 98; 42 T.L.R. 58; [1926] A.C. 37; 10 Tax Cas. 88.

Case referred to the High Court of Bombay by the Income-tax Appellate Tribunal, Bombay, under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by Section 92 of the Indian Income-tax (Amendment) Act, 1939 (VII of 1939), for decision of the following questions of law :

(1) Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment was not made in accordance with the provisions of Section 24B of the Income-tax Act and is for that reason invalid.

(2) Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment was validly made under Section 34 of the Act.

(3) Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment is invalid and can be called in question by the assessee on the ground that it was made without appointing an agent under Section 43."

Income-tax Reference No. 5 of 1942.

The facts of the case appear in the Statement of Case and judgment of the Appellate Tribunal.

JUDGMENT OF APPELLATE TRIBUNAL.

Under Section 33 of the Indian Income-tax Act (XI of 1922) the Income-tax Appellate Tribunal, M. MUNIR, President, N. R. GUNDIL, Judicial Member, and P. N. S. AIYAR, Accountant Member, delivered the following judgment :—

PRESIDENT.—“ This is an appeal by His Highness Maharaja Yadevindra Singh Maharajadhiraj Bahadur, Maharaja of Patiala, from the order of the Appellate Assistant Commissioner of Income-tax, ‘ A ’ Range, Bombay, passed on appeal from the order of the respondent by which he assessed for the assessment year 1937-38 the income that accrued in Bombay to the appellant’s father, His Highness Maharajadhiraj Sir Bhupindra Singh, the late Maharaja of Patiala.

2. The late Maharaja being a Ruling Prince was residing out of British India within the meaning of Section 42 of the Income-tax Act. He had some private property in several places and was deriving income from some other sources in British India, *e.g.*, from dividends, speculation and dealings in shares, and was being assessed in the past by different Income-tax Officers in British India through different officials of his State.

3. After the Income-tax Officer, Central Circle, Lahore, had determined the case for assessment for the year 1936-37, he received from the Commissioner of Income-tax, Punjab, N. W. F. and Delhi Provinces, an order to the effect that in consequence of the Allahabad High Court’s decision in the case of the *Maharaja of Benares*¹, the files of non-residents should be transferred “ to the Income-tax Officers in whose jurisdiction the non-resident’s own property or in whose jurisdiction the income arises so that those officers may try to appoint an agent connected with the source of income.” On receipt of this order the Income-tax Officer, Central Circle, Lahore, submitted the file of this case to this Commissioner for transfer to some other Income-tax Officer, and by the mutual consent of the Commissioner of Income-tax, Punjab, N. W. F. and Delhi Provinces, and the Commissioner of

Income-tax, Bombay, the file was transferred to the respondent, the Income-tax Officer, Non-Residents' Refund Circle, Bombay.

4. On 23rd November, 1938, the respondent, in keeping with the past practice which had been adopted in the time of the late Maharaja under the instructions of his Private Secretary, addressed the following letter to the Foreign Minister, His Highness's Government, Patiala :

"I have the honour to state that all the case papers of His Highness the Maharaja of Patiala have been transferred here from Lahore for information and necessary action. It is not easy to discover what has been done hitherto. So as a start I am sending the usual notices and beg to request that you will be good enough to let me have returns of income of His Highness from all sources in British India for the years ended 31st March, 1937 and 1938."

It is admitted that this letter was accompanied by a notice under Section 22 (2), Income-tax Act, addressed to "His Highness the Maharaja of Patiala" and required returns of income from all sources in British India for the two financial years ended the 31st March 1937 and the 31st March 1938. After some correspondence the required returns were filed—signed and verified by Mr. D. K. Sen, Foreign Minister on behalf of "His Highness the Maharaja of Patiala." The respondent in due course made the assessment for the year 1938-39 and the the year 1937-38, computing for the former year a net loss of Rs. 1,44,700 and assessing for the latter a taxable income of Rs. 3,43,097 and determining Rs. 50,337 to be the tax payable. On 11th October, 1940, the Foreign Minister wrote to the respondent to say that there had been a miscalculation in assessing the income for 1937-38 and that the correct amount of the tax due was Rs. 40,861-8 and not Rs. 50,337 as required by the notice of demand to be paid. The letter contained a request for a reconsideration of the assessment and revision of the notice of demand. Being doubtful about the respondent's power to revise the assessment the Foreign Minister, simultaneously with the letter of 11th October, 1940, and on the same grounds as were taken in that letter, appealed to the Appellate Assistant Commissioner, 'A' Range, Bombay, claiming as relief the reduction of the tax determined from Rs. 50,337 to Rs. 40,861-8. The respondent, acting under Section 35 of the Act, reduced the figure of taxable income from Rs. 3,43,097 to Rs. 3,10,461 and made the consequent reduction in the tax payable.

5. The appeal before the Appellate Assistant Commissioner presents a somewhat curious story. As stated above, the appeal dated 11th October, 1940, admitted the liability to tax to the extent of Rs. 40,861-8 and claimed a reduction of Rs. 9,475-8 on the ground of

an error in the calculations. Being free from all legal quibbles it was an honest and dignified document becoming the position of the party whom the respondent by his own wrong had driven for redress to superior authority. The appeal was not in the prescribed form and in the concluding paragraph contained the following prayer :

“ The notice of demand was received in this office on 20th September, 1940. As it will take some time to complete the necessary formalities, I request you kindly to extend the time limit of filing the appeal from 30 days to at least 90 days, failing which this letter may kindly be treated as a regular appeal and necessary action taken in the matter.”

There is no order of the Appellate Assistant Commissioner on this document showing whether the time for filing an appeal in the prescribed form was extended or not, or whether he had decided to treat this document itself as an appeal. On 22nd October, 1940, an appeal in the prescribed form, signed and verified by the Foreign Minister, was filed adopting the point raised in the appeal of 11th October as the first ground of appeal and containing the following as the second ground of appeal.

“ Attention is also invited in this connection to the judgment of the Allahabad High Court, vide *Aditya Narain Singh Bahadur v. Commissioner of Income-tax*¹ (Miscellaneous Case No. 52 of 1936 decided on 24th January 1938), which will show that His Highness the Maharaja of Benares was served with a notice about the assessment of tax on his income in British India and the High Court held that as no agent of the Maharaja, a non-resident of British India, had been appointed as required under Section 43 of the Income-tax Act, assessment could not be treated valid under Section 42 of the above Act, because of the defective service. According to this ruling the notice about the assessment of tax on His late Highness's income should have been served on an agent of His Highness in British India.”

6. On 27th February, 1941, a document purporting to be a “ petition of the Foreign Minister, Patiala, on behalf of His Highness the late Maharaja of Patiala ” was filed before the Appellate Assistant Commissioner containing two more grounds of appeal and asking for the setting aside of the order of assessment. These grounds were :

“ 3. The income purported to have been assessed was for the accounting year ended the 31st March, 1937, and the proceedings in respect of such income could have been initiated under Section 22 (2) of the Indian Income-tax Act, 1922, only during the year ended the 31st March, 1938. The Income-tax Officer, Non-Residents' Refund Circle, however, initiated such proceedings under Section 22 (2) of the

Act in November 1938. Further he did not issue and serve on the proper party the requisite notice under Section 34 of the said Act."

"4. H. H. the late Maharaja of Patiala died at Patiala on the 23rd March 1938. The notice under Section 22 (2) of the said Act, assuming that it was validly issued (it is not admitted) should have been issued and served upon the executor, administrator or other legal representative of H. H. the late Maharaja of Patiala. The notice, however, purported to be issued to 'H. H. the Maharaja of Patiala' and was sent to your petitioner with a covering letter dated 23rd October 1938. There was, therefore, no proper notice and no proper service of any notice. Consequently the return for the accounting year ended 31st March 1937 was submitted blank."

This petition was signed and verified by an officer of the Income-tax Department of the State, who had for his authority a certificate of authorisation under Section 61 of the Income-tax Act purporting to have been given by the appellant.

The certificate authorises the officer to produce accounts and documents and to obtain copies. Besides the omnibus clause "his explanation and statement will be binding on me" there is no provision in this certificate expressly authorising the officer to present or to verify an appeal.

7. All the grounds taken from time to time before the Appellate Assistant Commissioner were entertained and gone into by him and thus what was originally a simple and straightforward case was converted into a mere wrangle of technicalities. The Appellate Assistant Commissioner found that the Foreign Minister's original appeal of 11th October 1940 was a good appeal. He therefore reduced the taxable income by Rs. 31,319. The technical objections to the assessment, raised later, found no favour with him and were consequently repelled.

8. From the order of the Appellate Assistant Commissioner there is an appeal before us in which counsel for the appellant has not a word to say on the merits and the only ground for appeal is that the assessment is vitiated by the following irregularities of procedure:

"(1) that a dead man has been assessed without complying with the provisions of Section 24B (2);

(2) that the assessment has been made without serving a notice under Section 34; and

(3) that the appellant not being a resident in British India has been assessed without the appointment of an agent under Section 43."

Non-compliance with the provisions of Section 24B (2).

9. The case is governed by Section 24B (2) as it was before its amendment by the Amendment Act of 1939. That section is as follows:—

“Where a person dies before he is served with a notice under sub-section (2) of Section 22 or Section 34, as the case may be, the Income-tax Officer may serve on his executor, administrator or other legal representative a notice under sub-section (2) of Section 22 or under Section 34, as the case may be, and may proceed to assess the total income of the deceased person as if such executor, administrator or other legal representative were the assessee.”

10. Just as there cannot be a decree against a dead man, so under the Indian Income-tax Act, a dead man cannot be assessed. If the income of a dead man is to be assessed the procedure laid down by sub-section (2) of Section 24B must be followed. According to that sub-section, where a dead man's income is sought to be assessed, a notice under Section 22 (2) or Section 34, as the case may be, must be served on the executor, administrator or other legal representative of the deceased. It is implied in the sub-section that the notice should inform the person to whom it is addressed that the income of the deceased person whose executor, administrator or legal representative he is, is intended to be assessed. After service of the notice such person, qua the assessment of the income of the deceased person, becomes the assessee. On a plain reading of the sub-section it appears to me to be clear that its requirements are satisfied where the notice under Section 22 (2) is served on the legal representative, and on the service of such notice he understands the real issue, namely, that he is intended to be assessed in respect of a particular year's income of the deceased person whose legal representative he is.

11. The appellant is the legal representative of His Highness Sir Bhupindra Singh Sahib Bahadur, the late Maharaja of Patiala, whose income was intended to be assessed and has in fact been assessed in this case. The late Maharaja had died on 23rd March, 1938, whereas the notice under Section 22 (2) was not issued before 23rd November, 1938. What now has to be seen is whether this notice was in fact served on the appellant and whether he understood that the income of the late Maharaja for the financial year ended the 31st March, 1937, was intended to be assessed. After considering the facts on record and hearing the arguments of learned Counsel for the appellant I have little doubt in my mind that both the conditions were satisfied in this case.

12. The notice under Section 22 (2) that was issued on 23rd November, 1938, is admitted to have been addressed to “H. H. The Maharaja of Patiala” and was accompanied by a covering letter addressed to “the Foreign Minister, His Highness's Government, Patiala” (*vide* para. 4 of the petition dated 27th February 1941, presented to the Appellate Assistant Commissioner). At the time this notice was issued

the appellant was the ruling Maharaja. It is, therefore, fair to presume that the Foreign Minister, on receiving the notice, communicated to the appellant the contents of the notice which concerned the appellant personally and subsequently acted in the matter under the instructions of the appellant. The return that is signed and verified by him purports to be on behalf of "H. H. The Maharaja of Patiala." He could have no information about the personal income of the late Maharaja unless he derived such information from the appellant and he could hardly have undertaken the responsibility of filing a return without instructions from the appellant. After the assessment, professing to act on behalf of the appellants, he secured in the first instance from the respondent himself a substantial relief under Section 35 and later on from the Appellate Assistant Commissioner on appeal. In the assessment for the year 1938-39 he obtained not only a finding of no liability for the appellant but a finding of net loss amounting to Rs. 1,44,700. Throughout the proceedings he did not give the slightest indication that he had no concern with the matter and that the respondent should deal with the right person. For these reasons, I think, it must be held that not only the contents of the notice under Section 22 (2) were communicated by the Foreign Minister to the appellant but that the former throughout the proceedings acted in consultation with, and under the instructions of, the latter.

13. It is true that though the notice required the income of the financial year ended the 31st March, 1937, to be returned, it did not expressly state that the income to be returned was that of the late Maharaja. But it was all along understood both by the appellant and respondent that the income intended to be taxed was that of the late Maharaja.

At the time the notice under Section 22 (2) was issued the respondent did not know the name of the appellant or of his late father. When in the covering letter dated 17th October, 1939, that accompanied the return the Foreign Minister described the returned income as that of "His Highness Maharajadhiraj Mahendra Bahadur from all sources in British India for the years ended 31st March, 1937 and 1938," and respondent for the first time felt that the notice had perhaps been misunderstood and that the income of a wrong person had been returned. Therefore, by letter dated 15th December, 1939, he enquired from the Foreign Minister whether "Maharaja Mahendra Singh" was the name of the present Ruler or of his late father because his information related to the income that had accrued to Maharaja Bhupendra Singh in British India. He, however, omitted to notice that the income returned was, as is clear from the statement that was submitted with the

return, in fact the income of the appellant's father, His Highness Maharajadhiraj Sir Bhupendra Singh. This enquiry by the respondent brought the reply that Maharaja Mahendra Singh was the name of the appellant's great grandfather and that the name of the appellant was His Highness Maharajadhiraj Shri Yadevindra Singh Mahendra Bahadur. Notwithstanding this confusion of names, however, the real issue was clearly understood by all concerned, namely, that the income for the year ended the 31st March, 1937, of the then Maharaja of Patiala was intended to be taxed. The notice under Section 22 (2) required such income to be returned and the Foreign Minister acting for the appellant did return such income. Not only that but, as has already been pointed out in an earlier part of this order, the liability to pay a tax of Rs. 40,861-8-0 on an income of Rs. 2,78,535 was expressly admitted not only before the respondent but also before the Appellate Assistant Commissioner. The letter No. 2A—9900/35/95, dated 11th October, 1940, by the Foreign Minister to the respondent, and the petition of appeal of the same date to the Appellate Assistant Commissioner show beyond doubt that it was well understood by the Foreign Minister acting on behalf of the appellant that the income of the appellant's late father was being assessed through the appellant. It is true that in the order of assessment and in the petition of appeal to the Appellate Assistant Commissioner the assessee is described as the appellant's father but this is merely a misdescription showing nothing more than that the income of the appellant's father has been assessed. If the contention that a dead man has been assessed is correct it is equally correct that there could in that case be no appeal to the Appellate Assistant Commissioner by the Foreign Minister on behalf of the deceased Maharaja and no appeal by the appellant to us. It seems to be clear to me that it was fully understood that the appellant was being assessed in respect of the income of his late father for the year ended the 31st March, 1937, and that being so, it must, I think, be held that though there has been some confusion as to the manner in which the income of a dead man has to be reached by the tax-collector, the requirements of the law have in fact been fulfilled and the error or confusion, if any, not only does not vitiate the assessment but has not had the slightest effect on it.

Absence of notice under Section 34.

14. Coming now to the objection that a notice under Section 34 was not issued, the position is comparatively simple. The section (the case is governed by the old section) does not require a notice in any particular form. All that the section says is that if for any reason

income, profits or gains chargeable to income-tax have escaped assessment in any year, the Income-tax Officer may, at any time within one year of the end of that year, serve on the person liable to pay tax on such income, profits or gains a notice containing all or any of the requirements which may be included in a notice under Section 22 (2) and may proceed to assess or re-assess such income, profits or gains.

If, therefore, a notice in the form of a notice under Section 22 (2), or in any other form is served on the assessee within the time limited and it informs the assessee what income is intended to be assessed or re-assessed, the requirement of the section is satisfied. In this case the covering letter that accompanied the notice under Section 22 (2) stated that the respondent could not discover from the record whether the income for the relevant previous year had been assessed, and the respondent's note in red ink "we can only take action for 1937-38 and 1938-39" on the margin of the order sheet against the entry dated 10th October, 1938, in the Miscellaneous Record for 1936-37 shows that after receiving the record on transfer he did apply his mind to the question whether income for the year 1936-37 could at that time be assessed. The respondent can, therefore, be said to have had reasons to believe that in the year of assessment 1937-38, the income of the Maharaja had escaped assessment. This was sufficient justification for him to act under Section 34. The notice dated 23rd November, 1938, was served on the appellant within the time limited and this and the accompanying letter and the form clearly informed the appellant that the income of "the Maharaja of Patiala" for the year ended the 31st March, 1937, was intended to be taxed. It is settled law that notice under Section 34 need not be in any particular form; it is sufficient if it brings to the attention of the person to whom it is addressed the matters required to be answered or dealt with or the things required to be furnished. This requirement of the law also, was, therefore, complied with in this case.

Non-appointment of an Agent.

15. I now come to the last and the most important question in the case. It is contended that the appellant being not a resident in British India within the meaning of Section 42, Income-tax Act, he could, under that section, be only assessed in the name of an agent to be appointed under Section 43. Reliance is placed in support of this contention on a recent decision of the Allahabad High Court in the case of *The Maharaja of Benares*¹, which as already stated, was responsible for the transference of this case from the Income-tax Officer, Central Circle, Lahore, to the respondent, Income-tax Officer, Non-Residents' Refund Circle, Bombay. It has been held in

(1) (1938) 6 I.T.R. 217.

this Allahabad case is unmistakable terms that in the case of a non-resident it is the agent alone and not his non-resident principal that can be treated as the assessee, *i.e.*, the person to whom a notice under Section 22 (2) shall issue and by whom the tax is payable. The provisions of Section 42 (1), this case proceeds to lay down further, are mandatory and the department is precluded from issuing notices to the principal and from treating him as the assessee except to the limited extent that any arrears of tax may also be recovered from any of his assets which may be found in British India. This is the latest and the most fully argued out case on the point in which all previous authorities and English law have been discussed. The Appellate Assistant Commissioner has made a vain attempt to distinguish the present case from the Allahabad authority but the reasoning adopted by him in attempting to escape from the effect of that decision is poor argument which, I must say, we cannot even seriously consider. If there had been no other authority on the point binding on us, we would have had no option but to follow the Allahabad case and annul this assessment irrespective of what our personal view in the matter might have been. But we have staring us in the face the fact that in interpreting the law on the point the Allahabad High Court has differed not only from the Madras High Court but also from the Bombay High Court which is the court of reference in this case. A Special Bench of three Judges of the Madras High Court, following the decision of Mathew and Smith, JJ., in *Tischler v. Apthorpe*¹, which was approved by the Court of Appeal in *Werle & Co. v. Colquhoun*², has held that Section 42 of the Act is merely a machinery section by which the tax can be levied where the non-resident himself cannot be got at and does not lay down that the profits or gains are assessable to income-tax only in the name of an agent of the non-resident. This Madras case has been followed by the Bombay High Court in *Commissioner of Income-tax, Bombay v. National Mutual Life Association of Australasia*³, in which it has been held that a principal can be assessed under Section 42 of the Act without an agent being appointed under the latter part of that section. It is true that the point has not been fully discussed in that case but it did arise directly and the actual decision can be supported only on this view of Section 42. In this state of conflict of authority it would be presumptuous on my part to discuss the point at any great length. Suffice it to say that as a reference in this case would lie to the Bombay High Court, it is our obvious duty to follow the Bombay view leaving it to

(1) (1885) 52 L.T. 814 ; 2 Tax Cas. 89.

(2) (1888) 20 Q.B.D. 753 ; 2 Tax Cas. 402.

(3) (1933) 57 Bom. 519 ; 1 L.T.R. 350.

the appellant to seek a revision of that view from that Court itself. But in adopting that course I cannot help remarking that if the matter were *res integra* I would have taken the same view of this matter as has been taken in England and by the Madras and Bombay High Courts in India. If a non-resident assessee wishes to file a return of his income direct and to attend to the assessment proceedings himself, I do not see how the Income-tax Officer could say to him that he cannot assess him direct but must assess some one else for him, however ignorant of the former's various sources of income the latter may be. Yet that would be the precise result if the Allahabad view is correct—for a willing assessee the Income-tax Officer would have to get hold of some one else though he might be completely unaware of the non-resident assessee's means of income.

16. I must point out that we are not concerned in this case with the question whether an Income-tax Officer in British India is competent to serve notice under the Income-tax Act on a non-resident while he is out of British India and what are the consequences of non-compliance of such notices. We are dealing with a case where a notice in fact has not only been accepted but also gracefully complied with.

17. Before I take leave of this case I must mention that if this case which involves a substantial revenue is being decided in favour of the Crown it is solely due to the appellant's own willing attitude in the earlier stages of the case. As far as the Department is concerned, there has been no dearth of irregularities.

The case had been transferred to the respondent with the direction that he should appoint an agent for the assessee in accordance with the decision of the Allahabad High Court in the case of the Maharaja of Benares. Not the slightest attention seems to have been paid by the respondent to this direction by the Commissioner of the Punjab and N. W. F. and Delhi Provinces. Throughout the protracted proceedings and even after he was apprised of the death of Maharaja Bhupindra Singh he did not give a moment's thought to the legal question how the income of a dead man has to be assessed under the law. The way in which he has framed his order of assessment has provided ground for the argument that he has in fact assessed the deceased Maharaja through an official of the State who is neither his executor or administrator nor his legal representative. Though the case was one for the application of Section 34, not only did he not issue any notice under that Section in the usual form but he does not refer to that section at all in any part of the proceedings. The Appellate Assistant Commissioner by permitting several additional grounds of appeal converted a case of admitted liability into a case of contested liability. However

wide a discretion an appellate authority may have in permitting new grounds of appeal to be taken before him, it is, in my opinion, not a judicious exercise of that discretion to convert an honest straightforward case into an onslaught of technicalities on the officer making the original order to which not the slightest reference was made before him. If, therefore, I have ultimately held these proceedings to be regular, I must say, the finding is solely based on the framework of legality that is furnished in this case by the assessee's own conduct and admissions.

18. For the reasons given I would dismiss this appeal.

GUNDIL, Judicial Member.—I agree and have nothing to add.

P. N. S. AIYAR, Accountant Member.—I agree."

On the application of the assessee under Section 66 (1) of the Indian Income-tax Act (XI of 1922) the Appellate Tribunal (consisting of M. MUNIR, President, and A.L. SAGAL, Accountant Member), referred the case to the Bombay High Court.

STATEMENT OF CASE.

" This is an assessee's application under Section 66 (1), Income-tax Act, 1922, requiring the Tribunal to state to the High Court of Bombay certain questions, which, it is alleged, are questions of law and arise out of the order of the Tribunal under Section 38 of the Act in R.A.A. No. 29 (Bombay) of 1941-42.

2. The assessee is His Highness Maharaja Yadavindra Singh Maharajadhiraj Bahadur, the present Maharaja of Patiala, who had been assessed for the year of assessment 1937-38 under Section 34 of the Act in respect of the income that accrued in British India to his father His Highness Maharajadhiraj Sri Bhupindra Singh, the late Maharaja of Patiala.

3. The late Maharaja being a Ruling Prince was residing out of British India within the meaning of Section 42 of the Income-tax Act. He had some private property in several places and was deriving income from some other sources in British India, *e.g.*, from dividends, speculation and dealings in shares, and was being assessed in the past by different Income-tax Officers in British India through different officials of his State.

4. After the Income-tax Officer, Central Circle, Lahore, had determined the case for assessment for the year 1936-37, he received from the Commissioner of Income-tax, Punjab and N. W. F. and Delhi Provinces, an order to the effect that in consequence of the Allahabad High Court decision in the case of *Maharaja of Benares*¹, the

files of non-residents should be transferred "to the Income-tax Officers in whose jurisdiction the non-resident's own property or in whose jurisdiction the income arises so that those officers may try to appoint an agent connected with the source of income." On receipt of this order the Income-tax Officer, Central Circle, Lahore, submitted the file of this case to his Commissioner for transfer to some other Income-tax Officer, and by the mutual consent of the Commissioner of Income-tax Punjab and N.W.F. and Delhi Provinces and the Commissioner of Income-tax, Bombay, the file was transferred to the Income-tax Officer Non-Residents' Refund Circle, Bombay.

5. The late Maharaja died on 23rd March, 1938. On 23rd November, 1938, the Income-tax Officer, Non-Residents' Refund Circle, in keeping with the past practice which had been adopted in the time of the late Maharaja under the instructions of his Private Secretary, addressed the following letter to the Foreign Minister, His Highness's Government, Patiala :

"I have the honour to state that all the case papers of His Highness the Maharaja of Patiala have been transferred here from Lahore for information and necessary action. It is not easy to discover what has been done hitherto. So as a start I am sending the usual notices and beg to request that you will be good enough to let me have returns of income of His Highness from all sources from British India for the years ended 31st March, 1937, and 1938."

This letter was accompanied by a notice under Section 22 (2), Income-tax Act, addressed to "His Highness the Maharaja of Patiala" and required returns of income from all sources in British India for the two financial years ended the 31st March 1937 and the 31st March 1938. After some correspondence the required returns were filed—signed and verified by Mr. D.K. Sen, Foreign Minister, on behalf of "His Highness the Maharaja of Patiala." The Income-tax Officer in due course made the assessment for the year 1938-39 and the year 1937-38, computing for the former year a net loss of Rs. 1,44,700 and assessing for the latter a taxable income of Rs. 3,43,097, and determining Rs. 50,387 to be the tax payable. On 11th October 1940 the Foreign Minister wrote to the Income-tax Officer to say that there had been a miscalculation in assessing the income for 1937-38 and that the correct amount of tax due was Rs. 40,861-8-0 and not Rs. 50,387 as required by the notice of demand to be paid. The letter contained a request for a reconsideration of the assessment and revision of the Notice of Demand. Being doubtful about the Income-tax Officer's power to revise the assessment the Foreign Minister, simultaneously with the letter of 11th October, 1940, and on the same grounds as were taken

in that letter, appealed to the Appellate Assistant Commissioner, 'A' Range, Bombay, claiming as relief the reduction of the tax determined from Rs. 50,387 to Rs. 40,861-8-0. The Income-tax Officer, acting under Section 35 of the Act, reduced the figure of taxable income from Rs. 3,34,097 to Rs. 3,10,461 and made the consequent reduction in the tax payable.

6. The appeal before the Appellate Assistant Commissioner dated 11th October, 1940, admitted the liability to tax to the extent of Rs. 40,861-8-0 and claimed a reduction of Rs. 9,475-8-0 on the ground of an error in the calculations. The appeal was not in the prescribed form and in the concluding paragraph contained the following prayer :—

“The notice of demand was received in this office on 20th September, 1940. As it will take some time to complete the necessary formalities, I request you to kindly extend the time limit of filing the appeal from 30 days to at least 90 days, failing which this letter may kindly be treated as a regular appeal and necessary action taken in the matter.”

There is no order of the Appellate Assistant Commissioner on this document showing whether the time for filing an appeal in the prescribed form was extended or not, or whether he had decided to treat this document itself as an appeal. On 22nd October, 1940, an appeal in the prescribed form, signed and verified by the Foreign Minister, was filed adopting the point raised in the appeal of 11th October as the first ground of appeal and containing the following as the second ground of appeal :—

“Attention is also invited in this connection to the judgment of the Allahabad High Court, vide *Aditya Narain Singh Bahadur v. Commissioner of Income-tax*¹ (Miscellaneous Case No. 52 of 1936) decided on 24th January 1938, which will show that His Highness the Maharaja of Benares was served with a notice about the assessment of tax on his income in British India and the High Court held that as no agent of the Maharaja, a non-resident of British India, had been appointed as required under Section 48 of the Income-tax Act, assessment could not be treated valid under Section 42 of the above Act, because of the defective service. According to this ruling the notice about the assessment of tax on His late Highness's income should have been served on an agent of His Highness in British India.”

7. On 27th February, 1941, a document purporting to be a petition of the Foreign Minister, Patiala, on behalf of His Highness the late Maharaja of Patiala was filed before the Appellate Assistant Commissioner containing two more grounds of appeal and asking for the setting aside of the order of assessment. These grounds were :—

(1) (1938) 6 I.T.R. 217; A.I.R. 1938 All. 310.

"3. The income purported to have been assessed was for the accounting year ended the 31st March, 1937, and the proceedings in respect of such income could have been initiated under Section 22 (2) of the Indian Income-tax Act, 1922, only during the year ended 31st March, 1938. The Income-tax Officer, Non-Resident's Refund Circle, however, initiated such proceedings under Section 22 (2) of the Act in November, 1938. Further he did not issue and serve on the proper party the requisite notice under Section 34 of the said Act.

"4. H. H. the late Maharaja of Patiala died at Patiala on the 23rd March, 1938. The notice under Section 22 (2) of the said Act, assuming that it was validly issued (it is not admitted) should have been issued and served upon the executor, administrator or other legal representative of H. H. the late Maharaja of Patiala. The notice however, purported to be issued to 'H. H. the Maharaja of Patiala' and was sent to your petitioner with a covering letter dated 28rd October, 1938. There was, therefore, no proper notice and no proper service of any notice and consequently the return for the accounting year ended 31st March, 1937, was submitted blank."

This petition was signed and verified by an officer of the Income-tax Department of the State, who had for his authority a certificate of authorisation under Section 61 of the Income-tax Act purporting to have been given by the assessee.

8. All the grounds taken from time to time before the Appellate Assistant Commissioner were entertained and gone into by him. He found that the Foreign Minister's original appeal of 11th October 1940 was a good appeal. He therefore reduced the taxable income by Rs. 31,319. The technical objections to the assessment, raised later, found no favour with him and were consequently repelled.

9. From the order of the Appellate Assistant Commissioner an appeal was preferred to the Tribunal in which Counsel for the appellant did not have a word to say on the merits and the only ground for appeal was that the assessment was vitiated by the following irregularities:

(1) that a dead man had been assessed without complying with the provisions of Section 24B (2);

(2) that the assessment had been made without serving a notice under Section 34;

(4) that the appellant not being a resident in British India had been assessed without the appointment of an agent under Section 43.

10. The Tribunal dealt with and repelled all the grounds on which the validity of the assessment had been called in question and dismissed the appeal. The reasons which led the Tribunal to this conclusion are stated in detail in its order under Section 33.*

11. The assessee has now asked the Tribunal to refer to the High Court under Section 66 (1), Income-tax Act, the following questions :—

“(a) Whether in the circumstances of the case the appellant can be assessed without complying with the provisions of Section 24B (2) of the Income-tax Act.

(b) Whether in the circumstances of the case the assessment was legal, no notice having been issued under Section 34 of the Income tax Act.

(c) Whether in the circumstances of the case it is legal to make an assessment on the appellant, not being a resident in British India, without the appointment of an agent under Section 43 of the Income-tax Act.

(d) Whether in the circumstances of the case, the respondent had any jurisdiction to make the assessment on the appellant under the provisions of law.

(e) Whether in the circumstances of the case, the assessment is legal.

(f) Any other question of law that may arise out of the order of the Income-tax Appellate Tribunal.”

12. The Commissioner in his reply filed under Rule 54 of the Appellate Tribunal Rules states that the only questions of law that arise out of the Tribunal's order under Section 33 are as follows :—

“(a) Whether the assessment was validly made in accordance with the provisions of Section 24 B of the Act.

(b) Whether the assessment was validly made in accordance with the provisions of Section 34 of the Act.

(c) Whether in the circumstances of the case it is legal to make an assessment on the assessee not being a resident in British India without appointment of an agent under Section 43 of the Income-tax Act.”

13. Question (a) as formulated by the assessee in the application for reference assumes that the Tribunal in its order under Section 33 found that the provisions of Section 24B (2) had not been complied with. This assumption, however, is incorrect, inasmuch as the Tribunal on this part of the case found :—

(1) that the assessee was the legal representative of H. H. Bhupindra Singh Sahib Bahadur, the late Maharaja of Patiala, whose income was intended to be assessed and was in fact assessed ;

(2) that the contents of the notice under Section 22 (2), dated 23rd November, 1938, which was addressed to “H.H. the Maharaja of Patiala” and which was sent with a covering letter addressed to the Foreign Minister, His Highness's Government, Patiala, were

communicated by the Foreign Minister to the assessee and that throughout the subsequent proceedings, including the making of the return of income, the production of copies of accounts and the filing of an application under Section 35 and an appeal under Section 30 which resulted in a substantial reduction of the income of the assessee, the Foreign Minister acted in consultation with, and under the instructions of, the assessee; and.

(3) that the assessee understood that the income of the late Maharaja for the financial year ended the 31st March, 1937, was required by the notice under Section 22 (2) to be returned and that he was intended to be assessed in respect of that income.

On these findings the correct question of law that arises and which we refer to the High Court is :—

Whether in the circumstances found by the Tribunal in its order under Section 33 the assessment was not made in accordance with the provisions of Section 24B of the Income-tax Act and is for that reason invalid.

14. Question (b) as formulated by the assessee in the application for reference also proceeds on a misunderstanding of the Tribunal's order under Section 33, inasmuch as it assumes that no notice under Section 34 was issued in the case. On this part of the case the Tribunal definitely found :—

(1) that a notice under Section 22 (2) was served on the assessee;

(2) that the notice was served within the time within which a notice under Section 34 may be issued;

(3) that the notice informed the assessee that the income of the "Maharaja of Patiala" for the year ended the 31st March, 1937, was intended to be assessed; and

(4) that the notice was issued because the Income-tax Officer had reasons to believe that the income for the financial year 1936-37 had escaped assessment and after he had applied his mind to the question whether the income for that year could at the time be legally assessed.

The correct question, therefore, that arises out of the Tribunal's order under Section 33 on this part of the case and which we refer to the High Court is :—

"Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment was validly made under Section 34 of the Act."

15. The assessee and his late father, in respect of whose income the assessee has been assessed, were both residing out of British India

within the meaning of Section 42 of the Income-tax Act. The income that has been assessed occurred in British India and the assessment has been made without appointing an agent under Section 43 of the Act. The assessee not only did not object to his direct assessment, but willingly complied with the notice under Section 22 (2) and obtained a substantial relief by applying under Section 35 and appealing under Section 30 of the Act. The third question, therefore, that arises in the case and which we refer to the High Court is :—

“Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment is invalid and can be called in question by the assessee on the ground that it was made without appointing an agent under Section 43.”

16. Under Section 66 (1), Income-tax Act, 1922, we refer the following questions to the High Court of Bombay :—

“1. Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment was not made in accordance with the provisions of Section 24B of the Income-tax Act and is for that reason invalid.

2. Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment was validly made under Section 34 of the Act.

3. Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment is invalid and can be called in question by the assessee on the ground that it was made without appointing an agent under Section 43.”

These questions are subject to this statement of the case and the finding of fact in the Tribunal's order under Section 33.

17. The documents described in the Index will accompany this statement of the case.”

Sir Jamsheджи Kanga, for the assessee.

M. C. Setalvad with *G. N. Joshi*, for the Commissioner.

JUDGMENT.

BEAUMONT, C. J.—This is a reference made by the Income-tax Appellate Tribunal, Bombay, under Section 66 (1) of the Indian Income-tax Act, raising three questions. The questions all arise from certain technical defects alleged to exist in the order of assessment for the year 1937-38 of the estate of the late Maharaja of Patiala. The defects suggested are, first, that the terms of Section 24B of the Indian Income-tax Act were not complied with; secondly, that there was no notice under Section 34; and, thirdly, that no statutory agent had been appointed under Section 43. The material facts are these.

The late Maharaja of Patiala died on March 23, 1938, and the papers relating to the assessment on him were sent by the Commissioner of Income-tax of the Punjab to the Commissioner of Income-tax, Bombay, after the date of the Maharaja's death because of the decision of the Allahabad High Court, to which I will refer presently, which suggested that the estate of the late Maharaja could not be assessed unless a statutory agent were appointed under Section 43 of the Indian Income-tax Act. After the papers reached Bombay, some correspondence took place between the Income-tax Officer, Bombay, and a gentleman who is described as the Foreign Minister of the Patiala State, and eventually, in November, 1938, two notices were served on His Highness the Maharaja of Patiala, which in terms were issued under Section 22 (2) of the Indian Income-tax Act, one for the year 1937, and the other for the year 1938, requiring the Maharaja (that is, the present Maharaja) to make a return of his income. Returns were made of the late Maharaja's income, and on September 16, 1940, assessment orders for the respective years 1937-38 and 1938-39 were passed. In those orders the name of the assessee is stated to be "His Highness Maharajadhiraj Sir Bhupindra Singh," that is, the late Maharaja, and subsequently notices to pay were served on the Foreign Minister on behalf of the late Maharaja in the case of one notice, and of the present Maharaja in the case of the other.

I will deal first with the third question, which was first argued on behalf of the Commissioner. It is in these terms:

"Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment is invalid and can be called in question by the assessee on the ground that it was made without appointing an agent under Section 43?"

In view of the conflict which exists between High Courts in India on the question whether under the Act, before the amendment of Section 42 made in 1939, a foreign resident could be assessed direct upon income chargeable to income-tax under Section 4 (1) and Section 42 without appointing an agent under Section 43, I shall consider such question, in the first instance, without reference to the Indian cases.

Under Section 4 (1) of the Indian Income-tax Act before the amendment of 1939 it is provided:

"Save as hereinafter provided, this Act shall apply to all income, profits or gains, as described or comprised in Section 6, from whatever source derived, accruing or arising, or received in British India or deemed under the provisions of this Act to accrue, or arise, or to be received in British India."

That sub-section, it will be noticed, applies to persons wherever resident, provided the income is derived, or accrues, or arises, or is received in British India, or is deemed under the provisions of the Act to accrue or arise, or to be received in British India. Then Section 6 provides that "the following heads of income, profits and gains shall be chargeable to income-tax in the manner hereinafter appearing." Then various heads are stated, including "business." Then Sections 22 and 23 contain provisions for calling for returns and making assessments which apply to income falling within Section 4 (1), whether of a resident or non-resident.

Then we come to Section 42, which provides:

"In the case of any person residing out of British India, all profits or gains accruing or arising to such person, whether directly or indirectly, through or from any business connection or property in British India, shall be deemed to be income accruing or arising within British India, and shall be chargeable to income-tax in the name of the agent of any such person, and such agent shall be deemed to be, for all the purposes of this Act, the assessee in respect of such income-tax."

Then Section 43 enables the Income-tax Officer to appoint an agent for the purposes of Section 42. The first part of Section 42 appears to be a charging section, when read in connection with Section 4, because Section 4 makes taxable income which is deemed to accrue or arise, or to be received in British India, and Section 42 provides that certain income of a foreign resident shall be deemed to arise or accrue within British India. That part of Section 42 is a charging section. But the provisions for charging income upon an agent appear to me to be mere machinery, and that was so held by the Calcutta High Court in *Rogers Pratt Shellac & Co. v. Secretary of State for India*¹.

There is no doubt, reading Section 42 by itself, that at first sight there is a great deal to be said for the view that the only way in which income brought in to tax by that section can be charged is through an agent of the person entitled to the income, because the words are mandatory and provide that the income referred to *shall* be chargeable to income-tax in the name of the agent of any such person, and such agent *shall* be deemed to be the assessee for the purposes of the Act.

But I think the principle which has been established by certain English cases, *Tischler & Co. v. Apthorpe*² and *Werle & Co. v. Colquhoun*³, approved by the House of Lords in *Whitney v. Inland Revenue Commissioners*⁴ applies to the construction of Section 42. The English

(1) (1924) 52 Cal. 1.

(3) (1888) 20 Q.B.D. 753; 2 Tax Cas. 402.

(2) (1885) 52 L.T. 814; 2 Tax Cas. 89.

(4) [1926] A.C. 37; 10 Tax Cas. 88.

cases were decided on Section 41 of the English Income Tax Act of 1842, and, no doubt, there are distinctions between the wording of that section and the wording of Section 42, and, of course, the whole scheme of the English Income Tax Act is very different from the scheme of the Indian Income-tax Act. I would not rely on English cases for the purpose of construing particular words in the Indian Act, but I think the cases are important as establishing a general principle. The only substantial differences, as far as I can see, between Section 41 of the English Act and Section 42 of the Indian Act, are that Section 41 makes the non-resident chargeable in the name of the agent, whereas the Indian Act makes the income of the non-resident chargeable through the agent. Furthermore, the English Act has no provisions for appointing an agent such as are contained in Section 43 of the Indian Act; nor does the English Act say in so many words that the agent shall be deemed to be, for all the purposes of the Act, the assessee, although the English Act does provide that the agent is to perform the functions imposed upon an assessee by the Act. But admitting those distinctions, Section 41 of the English Act is a machinery section, and its terms are mandatory, and notwithstanding that, the English Judges, whilst admitting as I have admitted, that at first sight there is a good deal in support of the view that only the agent can be assessed, held that regard must be had to the object of the section, and that in authorising the assessment in the name of an agent the Legislature was giving a particular and additional power designed to meet an anticipated difficulty. The Legislature was enabling a foreign resident to be charged to income-tax, and the obvious difficulty, which was likely to arise, was that there would be no means of making the assessment, or of enforcing payment, because the foreign resident could not be got at. To get over that difficulty the Legislature provided that an agent within the jurisdiction might be assessed and charged to the tax. In the same way the machinery provided by Section 42 of the Indian Act, in my opinion, provides a special and additional power to meet a particular difficulty, and is not intended, and in the absence of clear words of prohibition, should not be construed, to take away existing powers. If the anticipated difficulty of assessing a non-resident does not arise, there seems no reason for insisting that the special means of assessment through an agent must be adopted. Suppose a case in which a non-resident, aware of the fact that he has derived income from a business connection in Bombay, and realising that he is liable to be taxed under Sections 4 and 42, but anxious to avoid the interposition of an agent, makes an offer to the Income-tax Officer in Bombay that if the Officer will tax him direct, he will fill up the necessary forms, attend

the office of the Income-tax Officer in Bombay, and produce any books that the Officer may require. If the Officer were to accept that offer, and make the assessment direct on the assessee under the provisions of Sections 22 and 23, could it seriously be suggested that the assessment was bad, and that the Income-tax Officer was bound to assess through the medium of an agent whom neither he nor the assessee desired to introduce? That would be a most unreasonable construction to put on the Act, and is not one I am prepared to adopt, unless obliged to do so by clear language. The mandatory terms of the machinery portion of Section 42 present no difficulty when once it is realised that such machinery is additional to the ordinary machinery. If the additional machinery is adopted, its terms must be followed, but it need not be adopted at all.

With regard to the authorities in India, the High Court of Madras as long ago as the year 1921 in *Chief Commissioner of Income-tax v. Bhanjee Ramjee & Co.*¹, held that a foreign resident being assessed under Section 42, or rather under the corresponding section of the Income-tax Act of 1918 which applied in that case, could be assessed without the interposition of an agent. That is a direct authority on this point. In *Commissioner of Income-tax, Bombay v. National Mutual Association of Australasia, Ltd.*², the question came before a bench of this Court of which I was a member. The question we had to consider was whether the Income-tax Officer had sufficient data to enable him to assess the assessee, who was an Insurance Company resident in Australia, without having recourse to a particular rule. The reference made by the Commissioner to this Court dealt only with the assessment under Section 4 (1), that is to say, the income had been assessed under Section 4 (1) without introducing Section 42. But on the reference the Advocate-General argued that, even if there were sufficient data to enable an assessment to be made under Section 4 (1), there was other income which could be assessed under Section 42, and that in respect of that income there was no sufficient data. This Court accepted that argument, and held that there was income of the foreign resident assessable under Section 42 in respect of which no sufficient data were supplied, and that was an essential part of our decision, because we thought that in respect of the income assessable under Section 4 (1) the data were sufficient. It was argued then that no assessment could be made under Section 42, because no agent had been appointed under Section 43, and on that question we followed the decision of the Madras High Court, and held that an assessment could be made under Section 42 without the interposition of an agent. I

(1) (1921) 44 Mad. 773.

(2) (1933) 27 Bom. 519; 1 I.T.R. 350.

myself in my judgment merely noted the decision and followed it without expressing agreement or disagreement, and it is my practice in construing an all-India statute to follow a decision of another High Court, which has not been dissented from. Mr. Justice Rangnekar expressed agreement with the decision. I may mention that that case subsequently went to the Privy Council, and the Privy Council held that the question under Section 42, not having been raised by the Commissioner, ought not to have been dealt with, and they declined to go into that question. So that, their decision leaves the decision of this Court, so far as it relates to the construction of Section 42, untouched. That was how the matter stood until the year 1938, when the matter came before the Allahabad High Court in *Maharaja of Benares v. Commissioner of Income-tax*¹, and the learned Judges refused to follow the rulings of the Madras and Bombay High Courts, and held that, even assuming that Section 42 was a machinery section, the provisions of the section made it compulsory to make an assessment on the non-resident under that section only through an agent. I have carefully reconsidered the question in the light of the reasoning of the Allahabad High Court, and for the reasons which I have given, I do not agree with the view of that Court, which, in my opinion, took too superficial a view of Section 42. Therefore, I think the answer to the third question is that the assessment is not invalid. It may be noticed that the unfortunate position introduced by the Allahabad decision, which results in one construction being put upon Section 42 in the United Provinces and a different one in Madras and Bombay, is only temporary, because under the amended Section 42 an assessment can be made in the name of the assessee or of the agent.

I will deal next with the second question, which is:

“Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment was validly made under Section 34 of the Act?”

Now, as I have already pointed out in stating the facts, notices were served on the Maharaja of Patiala under Section 22 (2) expressly, one notice in respect of the year 1937-38, and another in respect of the year 1938-39. The notice for the year 1937-38, not having been served until November 1938, was beyond time, as is admitted by the Tribunal; but the Tribunal think that being beyond time that notice can be construed as a notice under Section 34, for which it was within time, although unquestionably the notice in precisely the same form and served at the same time for 1938-39 cannot be construed as a notice under Section 34, partly because the year had not expired in that case, and partly because

(1) (1938) 6 I.T.R. 217; 1938 All. 432.

in the year 1938-39 there was a loss, and, therefore, there was no question that income had escaped assessment in that year. Now, I agree with the Tribunal that it is not necessary that a notice under Section 34 should assume any particular form, but it must give notice to the assessee that in the opinion of the Income-tax Officer some income has escaped assessment, and, as was held by the Privy Council in a recent case, *Commissioner of Income-tax, Bengal v. Mahaliram Ramjidas*¹ in order to justify a notice under Section 34, the Income-tax Officer must be *bona fide* of opinion that some income has escaped assessment. It is perfectly plain from the covering letter, which accompanied the notices under Section 22 (2), that in point of fact the Income-tax Officer knew nothing whatever about the matter, and did not consider the question whether any income had escaped assessment, and he had no more reason to believe that income had escaped assessment for 1937-38 than for 1938-39. For aught he knew both years might have resulted in a loss.

Mr. Setalvad argues on behalf of the Commissioner that we cannot take that view, because the Tribunal have found, as a fact, that the Income-tax Officer had reason to believe that the income for the year had escaped assessment. That finding might be challenged on the ground that there was no evidence to support it; but, apart from that, I am certainly not disposed to hold as a matter of law that, when a notice is given in terms under Section 22 (2), which subsequently turns out to be a bad notice under that section because it is out of time, it can be held automatically to be a good notice under Section 34, although there is no reason for supposing that the Income-tax Officer ever considered the question under Section 34. It seems to me quite clear that the notice in this case was not a notice under Section 34, and I decline to treat it as such. The second question, therefore, must be answered in the negative.

In view of that answer, the assessment is illegal, and the first question is really of only academic interest. The first question is:

“Whether in the circumstances found by the Tribunal in its order under Section 33, the assessment was not made in accordance with the provisions of Section 24B of the Indian Income-tax Act and is for that reason invalid?”

I observe in passing, with regret, that it seems from the wording of this question and others which have been submitted to us by the Tribunal that the Tribunal are adopting the practice followed by Subordinate Judges of framing issues in the negative, a practice which I have often condemned as inconvenient. A simple question “Is the assessment

valid " can be answered " Yes " or " No. " If the question be " Is the assessment not valid " or " not invalid ?, " a simple answer either in the affirmative or in the negative becomes ambiguous, and one has to look at the reasons to see what is meant. The question here is whether the assessment was not made in accordance with the provisions of Section 24B. If the question is answered in the negative, thus introducing a double negative, would it mean that the assessment was made in accordance with the section ? I hope that the Tribunal will abandon this practice of stating questions in the negative before it becomes a habit. However, I take the question as being whether the assessment was made in accordance with the provisions of Section 24B. Now, Section 24B deals with the assessment of a deceased person. In this case the person to be assessed was the late Maharaja, who had died before he was served with any notice under Section 22, and, therefore, the provisions of Section 24B (2) apply, and the Income-tax Officer was entitled to serve on the executor, administrator or other legal representative of the deceased Maharaja a notice under Section 22 (2) or under Section 34 as the case might be, and then proceed to assess the total income of the deceased Maharaja as if such executor, administrator or other legal representative were the assessee. As observed by the President of the Tribunal in his judgment, the Income-tax Officer made no attempt to observe the provisions of that sub-section. He served the notice on the present Maharaja, without showing in what capacity. But the Tribunal have found, as a fact, that the present Maharaja is the legal representative of the deceased Maharaja, and although it would obviously have been better so to describe him in the notice, I am not prepared to say that the notice was bad, if it was served on the legal representative, merely because it omitted to state that it was served in that capacity. It should have been stated that it was served on the legal representative of the late Maharaja, and that the return required was of the late Maharaja's income. It was not so stated, and the present Maharaja himself may have had taxable income for the years in question ; but I think there is a good deal of force in the contention of the Tribunal that any irregularities in this respect were waived by the Maharaja, because returns of the late Maharaja's income were made by the Foreign Minister on behalf of the Maharaja, and then subsequently corrections were made in the assessment at the instance of the Maharaja. There is no doubt that the present Maharaja knew perfectly well that what was being assessed was the income of his predecessor.

Then when one comes to the actual assessment, it is made on the deceased Maharaja. It is, of course, wholly irregular to assess a deceased person. The assessment should have been made on the legal

representative in respect of the income of the deceased. However, there again, the Patiala authorities seem to have accepted the view that it was an assessment made on the agent in respect of the income of the deceased person, because they have actually appealed against the assessment, and if the assessment was an assessment on a dead man, it was obviously a nullity, and there is nothing to appeal from.

On the whole, though I certainly do not wish to give any countenance to the idea that the provisions of Section 24B need not be strictly complied with, in the particular facts of this case, and having regard to the facts also that the question is merely of academic interest, having regard to the answer to the second question, I am prepared to say that the assessment, though not strictly made in accordance with the provisions of Section 24B, is in the circumstances valid so far as that section is concerned.

KANIA, J.—In this matter the accounting year is 1936-37 and the assessment year is 1937-38. The questions referred to us arise out of the income of the late Maharaja Sir Bhupindra Singh of Patiala. From the facts now on record it appears that His Highness had done certain business in shares and had also recovered certain dividends in respect of shares held in British India, in particular, in Bombay. The late Maharaja died on March 23, 1938. The late Maharaja had some properties in the Punjab and in respect of the income from the same the Income-tax Officer, Central Circle, Lahore, was making assessment orders. By virtue of a decision of the Allahabad High Court in *Maharaja of Benares v. Commissioner of Income-tax*¹, the Income-tax Officer, Central Circle, Lahore, thought that it was improper for him to make the assessment orders as according to that judgment he had no jurisdiction to do so. He, therefore, referred the matter to his superior officer, the Commissioner of Income-tax, Punjab and N.W.F. and Delhi Provinces. He pointed out that difficulties had arisen because of the decision of the Allahabad Court and requested that as it appeared that the late Maharaja had some income in Bombay, the papers may be sent to Bombay so that an agent may be appointed and the assessment proceedings adopted in Bombay. On that the Commissioner of Income-tax, Delhi, sent over the papers to the Commissioner of Income-tax, Bombay Presidency, Sind and Baluchistan, and they were evidently received here on or about November 14, 1938. The Commissioner of Income-tax, Bombay, sent the file to the senior Income-tax Officer, Bombay, who, on November 23, 1938, wrote the following letter to the "Foreign Minister, His Highness's Government, Patiala":—

"I have the honour to state that all the case papers of His Highness the Maharaja of Patiala have been transferred here from Lahore for information and necessary action. It is not easy to discover what has been done hitherto. So, as a start I am sending the usual notices and beg to request that you will be good enough to let me have the returns of income of His Highness from all sources in British India for the years ended March 31, 1937, and 1938."

Along with that he had sent two printed notices which were headed "under Section 22 (2) and Section 38 of the Income-tax Act." They were addressed to "His Highness the Maharaja of Patiala," and by paragraph 2 the addressee was called upon to send a return of the total income from all sources during the previous year, *i.e.*, twelve months ending March 31, 1937, and in the other notice for twelve months ending March 31, 1938. Two returns signed by the Foreign Minister in response to those notices were sent to Bombay. The return for 1937 was blank; the other, for 1938-39, had certain figures written against item No. 5, *viz.*, business, trade, commerce, manufacture or dealing in property, shares or securities, etc. At the foot of the first return it was stated "This period also is covered by the attached return" (*i.e.*, the other return). Subsequent correspondence followed in which at the request of the Bombay Income-tax Office items were disclosed to show what was the income during 1937-38 and what was the income (which in fact was the loss) during 1938-39. Following these, two assessment orders, dated September 10, 1940, were passed. Against the name of the assessee in both of them is written "His Highness Maharaja Sir Bhupindra Singh late Maharaja of Patiala." The notice (which is the usual thing printed on the front part) is addressed to the Foreign Minister on behalf of His Highness the late Maharaja of Patiala.

Subsequent representations were made by the Foreign Minister to the Income-tax Officer to reduce the amount assessed on the ground of mistake and an appeal was preferred to the Assistant Commissioner for a further reduction of the amount. In both of these there was a partial success. On October 22, 1940, the Foreign Minister sent the grounds of appeal in the prescribed form in which he raised in effect the three questions which are now before the Court. The matter was first considered by the Tribunal, and in the course of their judgment the Tribunal held that there was gross irregularity in the matter of this assessment, but as in fact substantial justice was done, they recorded their findings against the assessee.

The first question is in respect of application of Section 24B. That section gives rise to two considerations: (1) whether the notice required to be served was served on the legal representative of the

deceased assessee; and (2) whether the assessment was made on the total income of the Maharaja as such legal representative of the assessee. On the first question on looking at the notice it is clear that it is addressed only to His Highness the Maharaja of Patiala. It does not on its face disclose whether it was intended for the late Maharaja or for the ruling Maharaja. It does not refer at all to any legal representative of any party. On behalf of the Commissioner it was argued that the section requires that a notice should be served on the legal representative and it was not necessary that on its face it should be addressed to the legal representative. It was contended that it was therefore sufficient if it was in fact served on the legal representative and was understood by the party receiving it as served on him in that character. I think there is considerable force in that contention, particularly in the present case as on the facts on record the present Maharaja had not disputed the validity of the notice till the matter finally came before the Tribunal. The second point, however, appears to be more difficult to get over at first sight. The assessment order clearly discloses the name of the late Maharaja Sir Bhupindra Singh as the assessee, and that is certainly bad. But the notice directing payment is addressed to the Foreign Minister and thereafter proceedings were adopted by the Foreign Minister evidently under instructions from the present Maharaja. In the matter of this assessment having regard to all the circumstances, although there is gross irregularity, if other things were against the assessee, on this ground alone I would not have perhaps disturbed the assessment order. I must however put on record my opinion that the issue of the assessment order in the name of the late Maharaja was highly irregular and should not in the ordinary course and circumstances be validated lightly.

The second question relates to Section 34 of the Act, and the question is whether the notice given to the Maharaja on November 23, 1938, was in fact a notice under that section. It may be noted that two notices were sent on the same day to the same party. They are on exactly similar printed forms and there is nothing to show as between the two, that one was under Section 22 (2) as appears printed on the top of the notice, while the other with the same things printed on the top of the notice was served as a notice under Section 34. I should point out that the two printed notices are correctly the only notices which are issued under the Act and the covering letter in this connection which is addressed to the Foreign Minister and not the Maharaja should be disregarded. However if the covering letter is also looked at, it does not assist the Commissioner's case. That letter without any distinction between the notices given for the assessment years 1937-38

and 1938-39 calls upon the addressee to send the returns. The Commissioner's argument is that simply because the notice in respect of the assessment year 1937-38 was sent after the expiry of one year the Court must hold that it was a notice under Section 34. I am not prepared to accept that argument. There is no justification for assuming that a notice which on the top of it states that it was under Sections 22 (2) and 38 should, because it is served after a year, be treated by the assessee as a notice under Section 34, when the officer issuing the notice had given no indication that it was a notice under Section 34. If the Income-tax Officer proposes to act under Section 34, when the notice is served on him the assessee is entitled to know that the Income-tax Officer is taking steps under that section. That can certainly not be conveyed by a service of a printed notice only headed under Sections 22 (2) and 38. In my opinion, therefore, on a construction of the words of this printed notice read if necessary along with the covering letter, the Commissioner's argument that a notice under Section 34 was served is unsound.

Mr. Setalvad relied on certain observations in *Jawala Prasad v. Commissioner of Income-tax*¹. In that case the question for the Court's consideration was, "whether, having regard to the fact that Section 34 of the Act requires 'particulars' to be stated in the notice and that the notice is the basis of the proceedings under the said section, the Income-tax Officer was competent in law to go behind the particulars as specified in the notice." In dealing with the point Costello, J., observed (p. 303):

"Therefore, so long as it brings to the attention of the person to whom it is served the matters required to be answered or dealt with or the things required to be furnished it is sufficient."

From this it was argued that if a notice containing all the particulars under Section 22 (2) was served on the assessee, the assessee had notice of what he was required to give by way of information and therefore the notice was sufficient. I am unable to read the observations of that learned Judge with such meaning at all. The learned Judge was dealing with the question whether a notice clearly given under Section 34 requiring certain particulars to be given conveyed to the assessee what particulars were called for. The observations are not general, and in my opinion it is wrong to read them in the general sense without reference to the context. In view of this finding the assessment made on the footing of this notice is invalid, and the answer to that question must be as stated in the judgment of the learned Chief Justice.

The third question gives rise to a somewhat intricate question of law on which there has been a difference of opinion in India. Section 4 of the Act states what incomes are liable to be assessed. Section 42 (first part) ropes in certain further income of a non-resident, who is liable to be assessed. Then that section (by the second part) provides that the income shall be chargeable to income-tax in the name of the agent of such person and the agent shall be deemed to be for the purposes of the Act the assessee in respect of such income-tax. From these words it is argued on behalf of the assessee that the non-resident assessee is not liable to be taxed directly in any circumstances and it is obligatory on the taxing officer to assess the agent only. In reply to the question, "What happens if there is no agent?" it is suggested that under Section 43 the taxing officer has jurisdiction to appoint an agent. At first sight there appears to be considerable force in this contention, but a closer scrutiny shows that the contention is not correct. We have to construe the section before its amendment in 1939. The first part of Section 42 is a charging section, according to the decisions of all Courts. If one reads that section as an independent section, to put at its highest according to the assessee's contention, only for that income the agent would be exclusively taxable. The result therefore would be that in respect of a non-resident's income liable to be taxed under Section 4 he himself can be taxed, while in respect of the income covered by the first part of Section 42 the agent alone will be liable to tax. In the normal course such an interpretation should be avoided. If a person is himself available for taxation, it will require a very clear provision of law to hold that although he is present and willing to be taxed, his agent alone should be taxed. In fact that will be taking away from the principal his elementary right, when he is the party who is liable to pay, and compelling him to appoint an agent when he may be unwilling to do so all along. The proviso to the section is relied upon as supporting the contention, but in my opinion that argument is unsound. The proviso only deals with the contingency of no fund being found from which the tax could be recovered. In such a case it will be open to the taxing officer to recover the tax from funds which may be subsequently found within British India belonging to the assessee.

As regards the judicial interpretation of this section the Madras High Court in *Chief Commissioner of Income-tax v. Bhanjee Ramjee & Co.*¹, held that this section was only a machinery section, to recover tax on income which a non-resident was liable to pay, and it did not exclude the liability of the non-resident himself to be taxed if the

(1) (1921) 44 Mad. 773; 1 I.T.C. 147.

taxing officer could reach him. That view was approved by Rangnekar, J., expressly in *Commissioner of Income-tax, Bombay v. National Mutual Association of Australasia Ltd.*¹ In terms the learned Chief Justice has not recorded his approval but the basis of the decision can be assumed to be the approval of that interpretation. In *Rogers Pratt Shellac & Co. v. Secretary of State for India*², the later part of the section was considered a machinery to recover the tax. In *Maharaja of Benares v. Commissioner of Income-tax*³, (the decision under which the records of this case were sent over from Lahore to Bombay) the Allahabad High Court, differing from the view of the Madras High Court, held that in respect of non-residents, under Section 42 the agent alone had to be taxed and they relied in particular on the concluding words of Section 42. This Court has repeatedly affirmed that in the matter of interpretation of an All-India Act if other High Courts have adopted a particular construction it is desirable to adopt that even if the Court had some doubt about its correctness. But here there is a divergence of view between the Allahabad and Madras High Courts. This Court has adopted the interpretation of the Madras High Court in *Commissioner of Income-tax, Bombay v. National Mutual Association of Australasia Ltd.*¹

Apart from the decisions I think that the interpretation put on the words of this section by the Madras High Court and expressly adopted by Rangnekar, J., is correct. Although considerable stress was laid in the course of argument advanced on behalf of the assessee on the distinction between the English Act and the Indian Act, and it was pointed out that the schemes of the two Acts were different, and that there were no words in the section of the English Act corresponding to the concluding words in Section 42, it seems to me that far stronger words are required to deprive the taxing authorities of their rights to resort to the ordinary machinery of taxing which is permissible to be adopted in respect of the income under Section 4. As pointed out in the cases referred to by the learned Chief Justice, the English Courts for over forty years had affirmed that the corresponding section in the English Act was a machinery section. It is also held that it is an enabling section and gives an additional power to the Crown to collect the assessment. It is not a disability as contended by the assessee in this case. That principle of construction, irrespective of the actual words used, appears to be sound and I do not think that by the use of words differently placed in this section that principle is given a go-by by the Indian Legislature in framing Section 42. I, therefore,

(1) (1933) 57 Bom. 519; 1 I.T.R. 350,

(2) (1924) 52 Cal. 1,

(3) (1938) All. 432; 6 I.T.R. 217.

respectfully differ from the view of the Allahabad High Court and adopt the interpretation put on the construction of Section 42 as noted by the Madras and the Calcutta High Courts and accepted by Rangnekar, J. It may be noticed that the amended section adopts this view. The answer to the third question therefore will be as stated in the judgment of the learned Chief Justice.

PER CURIAM.—With regard to costs, the Tribunal has raised three questions, one of which, and the one no doubt which occupied most time, is answered in favour of the Commissioner, another of which is answered against him, and the third of which is answered in his favour, though with considerable criticism as to the conduct of his department. The net result is that the assessee succeeds, because on the answer to the one question in his favour the assessment will have to be set aside.

In dealing with the costs of a reference made by the Tribunal, we must have regard to the number of questions raised, their complexity, the evidence involved, and the conduct of the parties. The ultimate effect of the answers is not our concern. In the present case we cannot ignore the fact that two of the questions raised were necessitated by the conduct of the Income-tax Officer in ignoring the terms of the Act, and though the Commissioner has succeeded on two questions out of three, we think it right to make no order as to costs; each side to pay its own costs.

Reference answered accordingly.

[IN THE CHIEF COURT OF OUDH.]

RANI ANAND KUNWAR

v.

COMMISSIONER OF INCOME-TAX, C.P. AND U. P.

THOMAS, C.J., and BENNET, J.

February 8, 12, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 14 (1)—HINDU UNDIVIDED FAMILY—IMPARTIBLE ESTATE REGULATED BY OUDH ESTATES ACT—WIDOW OF PREVIOUS HOLDER—WHETHER MEMBER OF HINDU UNDIVIDED FAMILY—MAINTENANCE ALLOWANCE PAID TO SUCH WIDOW UNDER DEED—WHETHER EXEMPT FROM TAX.

The holder of an impartible estate regulated by the Oudh Estates Act executed two deeds in favour of the assessee, the widow of a previous holder, under which the assessee was to receive an allowance of Rs. 2,500 a month as maintenance and Rs. 500 a month as pilgrimage and other

expenses. The assessee claimed that she received the allowances as a member of a Hindu undivided family and they were therefore exempt under Section 14 (1). In reply to an enquiry of the Income-tax authorities, the holder of the estate stated that the assessee was not a member of a Hindu undivided family and she had no right or share in the estate. On a reference under Section 66 (3) :

Held, (1) that the question whether a person is or is not a member of a Hindu undivided family is primarily a question of fact ;

(2) that the estate was not held by a Hindu undivided family, but by a single holder under the Oudh Estates Act ;

(3) that, under the circumstances, the assessee was not a member of a Hindu undivided family within the meaning of Section 14 (1).

Cases referred to :—

Commissioner of Income-tax, Bombay *v.* Laxminarayan (1935) 59 Bom. 618 ; 3 I.T.R. 367 ; 8 I.T.C. 239 ; A.I.R. 1935 Bom. 412 ; 37 Bom. L.R. 692.

Commissioner of Income-tax, Madras *v.* Narayana Gajapathi Raju Bahadur Garu (1934) 2 I.T.R. 288 ; A.I.R. 1934 Mad. 608 ; 57 Mad. 1023 ; 67 M.L.J. 306 ; 7 I.T.C. 304.

Commissioner of Income-tax, C.P. and U.P. *v.* Rudh Kumari (1940) 8 I.T.R. 607 ; 1940 O.W.N. 853.

Commissioner of Income-tax, Bihar & Orissa *v.* Sir Rajendra Narayan Bhanja Deo of Kanika (1938) 6 I.T.R. 536 ; A.I.R. 1938 Pat. 611 ; 1938 P.W.N. 801 ; 19 P.L.T. 858.

Commissioner of Income-tax, Bihar & Orissa *v.* Visheshwar Singh (1935) 3 I.T.R. 216 ; A.I.R. 1935 Pat. 342 ; 156 I.C. 116 ; 14 Pat. 785.

Kunwar Kartar Singh *v.* Commissioner of Income-tax, Punjab (1937) 5 I.T.R. 569 ; A.I.R. 1937 Lah. 905.

Makhan Lal Ram Sarup, *In re* (1925) A.I.R. 1925 All. 298 ; 86 I.C. 27 ; 1 I.T.C. 416.

Case stated under Section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, C. P. and U. P., for the decision of the following question :—

“ Whether the assessee is a member of a Hindu undivided family within the meaning of Section 14 (1) of the Act ; and, if so, whether she received the maintenance allowance in dispute in such capacity.”

Civil Reference No. 5 of 1941.

STATEMENT OF CASE.

“ In compliance with your Lordships’ order, dated the 28th September 1939* in Income-tax Case No. 2 of 1936 I have the honour to submit, for your Lordships’ decision, under Section 66 (3) of the Indian Income-tax Act, 1922 (hereinafter referred to as “ the Act ”), the question of law formulated in paragraph 4 below and arising out of the assessments for the years 1934-35 and 1935-36 of Shrimati Rani Anand Kunwar of Lakhimpur, district Kheri (hereinafter referred to as “ the assessee ”). I regret the delay which has occurred in submitting this statement. A hearing was given to the learned Advocate

* Reported in *Rani Anand Kunwar v. Commissioner of Income-tax, C.P. & U.P.* (1940) 8 I.T.R. 126.

for the assessee on the 14th March 1940 and a draft of the statement was prepared shortly thereafter and it was later sent to, and approved by, the assessee. A difficulty, however, then arose as certain material facts were not clear from the records. A further investigation of such facts had to be made and copies of certain relevant documents obtained. An unavoidable delay occurred in this connection and it was only very recently that the investigation was completed and the facts elucidated.

2. **Facts of the Case.**—In the financial year 1935-36, the Income-tax Officer, Sitapur Circle, who has jurisdiction over the entire district of Lakhimpur-Kheri also, enquired from Shriman Raja Yuvraj Dutt Singh Sahib, Taluqdar of Oel and Kaimarah estates (hereinafter referred to as “the present Raja”), the names of the persons who received maintenance allowance (*guzara*) from the estate. The Manager of the estate, in reply, sent a list of *Guzaradars* of the Oel estate on the 27th August, 1935. In this list the assessee, who is the widow of the late Raja Krishna Dutt Singh, paternal grandfather of the present Raja, was shown as having received Rs. 30,000 as *guzara* allowance and Rs. 6,000 as pilgrimage expenses in 1934-35 and Rs. 25,583-5 and Rs. 5,116-10 respectively on the same accounts in 1933-34. The Income-tax Officer then enquired from the present Raja whether the *guzaradars* noted in the list supplied by the Manager of the estate were members of his joint family and whether they had any right or share in his estates in lieu of which the *guzara* allowances were paid to them. A copy of this letter, dated the 2nd September, 1935, is attached as Exhibit A. The present Raja replied that the *guzaradars* noted in the list were not members of a joint Hindu family and had no right or share in the estates. He further said in the same letter that the estates which he held were impartible and devolved on him as the sole heir and legatee of his grandfather, Raja Krishna Dutt Singh (hereinafter referred to as “the late Raja”). A copy of this letter dated the 16th September, 1935, is appended as Exhibit B. The Income-tax Officer thereupon issued two notices to the assessee—one under Section 22 (2) of the Act for the year 1935-36, in which the income of the previous year 1934-35 fell to be assessed, and the other under Section 22 (2) read with Section 34 of the Act for the year 1934-35, in which the income of the previous year 1933-34 fell to be assessed. The assessee complied with both the notices and returned an income of Rs. 36,150 for 1935-36 (Rs. 36,000 from *guzara* and Rs. 150 from property) and Rs. 30,849-15 for 1934-35 (Rs. 30,699-15 from *guzara* and Rs. 150 from property). The Income-tax Officer accepted these returns and made the assessments accordingly, under Section 23 (1) of the Act, on the 31st December, 1935, on an income of Rs. 36,000 for 1935-36 and

Rs. 30,700 for 1934-35. But by oversight he omitted the income from property in both assessments. Each of the assessment orders is in the following brief terms:—

“Return of income accepted and assessment made accordingly under Section 23 (1).”

The assessee appealed to the Assistant Commissioner against both the assessments and contended that the *guzara* which was received from her grandson, the present Raja, under two deeds of agreement, dated the 30th December, 1932, was not liable to tax under the Act, as it was a charge on certain villages of the Oel estate and as such should be held to be “agricultural income” and also because she received the *guzara* as a member of a Hindu undivided family. The Assistant Commissioner gave no finding on the first point, *viz.*, that the *guzara* was exempt as being “agricultural income”; but he decided the second point, *viz.*, that the assessee received the *guzara* as a member of a Hindu undivided family, against the assessee and dismissed both the appeals. A copy of his order, dated the 8th July, 1936, which covered both appeals, is appended as Exhibit C.

The assessee then filed an application before my predecessor and asked him to cancel the assessments in exercise of his revisional powers under Section 33 of the Act, or, in the alternative, to refer the questions of law which arose in the case to your Lordships for decision under Section 66 (2) of the Act. A copy of this application is appended as Exhibit D. My predecessor, however, holding that no reference lay to the Chief Court under Section 66 (2) of the Act in the circumstances of the case, rejected the application. A copy of his order, dated the 30th October, 1936, is appended as Exhibit E.

The assessee thereupon moved an application before your Lordships under Section 66 (3) of the Act and as a result your Lordships have been pleased to direct me to make this reference. Copies of the assessee's application and of your Lordships' order thereon* are appended as Exhibits F and G respectively.

3. The circumstances under which the *guzara* allowances were paid to the assessee in the years 1933-34 and 1934-35 were as follows:—

While the estate was under the management of the Court of Wards, the late Raja, who was at that time the holder of the estate, executed a will on the 3rd June, 1927. A translation of this will is appended as Exhibit H. By clause 5 of this will the assessee was to receive a maintenance allowance of Rs. 1,000 a month. But even before the late Raja's death the assessee was receiving an annual allowance for

*Reported in *Rami Anand Kunwar v. Commissioner of Income-tax, C.P. and U.P.* (1940) 8 I.T.R. 126.

maintenance, pilgrimage expenses, charity, etc. It has been ascertained from the Court of Wards' office that such allowances were paid to her as follows:—

| Period. | Maintenance allowance | Pilgrimage expenses, charity, etc. | Miscellaneous | Total. |
|-------------------------------------------------------------------------------------------------------|----------------------------------|------------------------------------------------------------------------------------------------------|---------------|--------|
| | Rs. | Rs. | Rs. | Rs. |
| 1st October, 1927 to 30th September, 1928 | ... } *15,200 | *2,000 | 1,926 | 19,126 |
| 1st October, 1928 to 30th September, 1929 | ... } 12,300 | 1,275 | 4,835 | 18,110 |
| 1st October, 1929 to 30th September, 1930 | ... } 12,000 | 1,500 | 3,827 | 17,327 |
| 1st October, 1930 to 30th September, 1931 | ... } 12,000 | 1,500 | 8,143 | 21,643 |
| 1st October, 1931 to 30th September, 1932 and 1st October, 1932 to 23rd April, 1933 | ... } ... } ... } ... } | Figures are not available as the relevant ledgers could not be traced in the Court of Wards' office. | | |

* These amounts appear to include some arrears of a prior period.

The late Raja died on the 15th December, 1932, and was succeeded by his grandson, the present Raja. On the 30th December, 1932, the present Raja executed two deeds in favour of the assessee whereby the latter was to receive Rs. 2,500 a month as maintenance allowance and Rs. 500 a month for pilgrimage expenses, charity, etc., and these were to remain as a charge on certain villages of the estate. Translations of these deeds are appended as Exhibits I and J. These deeds became operative from the 24th April, 1933, the date on which the estate was released from the Court of Wards. During the year 1933-34, therefore, the assessee received, as stipulated by the deeds, a sum of Rs. 25,583-5 for *guzara* and a sum of Rs. 5,116-10 for pilgrimage expenses (totalling Rs. 30,699-15). These are proportionate figures for a period of 10 months and 7 days, i.e., from 24th April, 1933, to 28th February, 1934, (the allowance for March, 1934, falling in the next year 1934-35). In the year 1934-35 again the assessee similarly received Rs. 36,000 for the full period of twelve months. It may be mentioned here that later

on in the year 1938-39 disputes again arose between the assessee and the present Raja and eventually a compromise decree for the payment of maintenance was passed by the Civil Court. But we are not at the moment concerned with those events.

4. **Question of Law.**—The question of law which is to be referred to your Lordships for decision has not been formulated in your Lordships' order. In the assessee's application to the Commissioner under Section 66 (2) of the Act, however, the question of law which was sought to be referred was formulated in the following terms :—

“Whether the petitioner could be considered to be a member of a Hindu undivided family as contemplated by Section 14 of the Act and whether as such the maintenance allowance received by her was not exempt from taxation.”

The question was repeated in the same terms in paragraph 6 (f) of the assessee's application under Section 66 (3) of the Act to your Lordships. Accordingly it is this question which must be regarded as the question in issue and the question of law which is referred for your Lordships' decision is therefore framed in the following paraphrased form :—

“Whether the assessee is a member of a Hindu undivided family within the meaning of Section 14 (1) of the Act ; and, if so, whether she received the maintenance allowance in dispute in such capacity ? ”

If your Lordships' answer to both parts of the question is in the affirmative the maintenance allowance will be exempt under Section 14 (1) of the Act.

5. **Opinion of the Commissioner.**—It is necessary at the outset to consider the status of the present Raja from whose estate the maintenance allowance was received by the assessee. The estate is an impartible estate and the present Raja is for the time being the sole owner of it. There is no dispute about this. I submit therefore that, according to the decisions of the Patna High Court in *Raja Shiva Prasad Singh*¹ and *Sir Rajendra Narayan Bhanja Deo of Kanika*² and of the Madras High Court in *Raja of Bobbili*³ the present Raja is liable to be assessed in respect of the income of the estate as an individual and not as a Hindu undivided family.

On the question whether a Hindu widow or other female person is a member of a Hindu undivided family within the meaning of the term as used in the Income-tax Act, I need do no more than refer to a recent decision of your Lordships in *Shrimati Rani Rudh Kumari*⁴ where it was held that females entitled to maintenance under the Hindu law can be members of a Hindu undivided family. In one

(1) (1925) 1 I.T.C. 384.

(2) (1938) 6 I.T.R. 536.

(3) (1937) 5 I.T.R. 79.

(4) (1940) 8 I.T.R. 607.

respect, however, that case differs from the present case. Here we have an impartible estate of which Raja Yuvraj Dutt Singh is the sole owner. As will be observed from Exhibits A and B annexed hereto an inquiry made from him as to whether the present assessee was a member of a Hindu undivided family evoked an answer in the negative. It is submitted that this provided sufficient material to justify the finding that the assessee was not a member of a Hindu undivided family.

The answer to the first part of the question of law formulated above is therefore, I submit, in the negative.

As regards the second part of the question, this will arise only if your Lordships' answer to the first part is in the affirmative. If the assessee was a member of a Hindu undivided family she was no doubt entitled to maintenance; but even if she had such right she must be deemed to have renounced it as soon as she entered into an agreement with the present Raja by the execution of the two deeds of the 30th December, 1932. I submit that after this date the right to receive the maintenance allowance derives from the deeds and not from her membership of the family. The terms of these deeds, as well as the will of the late Raja, support this view. Clause 4 of the will shows that the late Raja had a suspicion in his mind that after his death an attempt might be made by some interested persons to dispute the title of Yuvraj Dutt Singh, the present Raja, to the estate. For this reason he clearly mentioned in the will that, even if such an attempt should prove successful, the will would remain operative in favour of Yuvraj Dutt Singh. This very suspicion is again alluded to in the deed of the 30th December, 1932, executed by the present Raja whereby the maintenance allowance of the assessee was increased to Rs. 2,500 a month. The body of this deed recites that the present Raja is entitled under the late Raja's will to inherit all the property and rights belonging to the late Raja. The assessee as a party to this deed therefore recognized such title of the present Raja. Clause 5 of the same deed further provides that the assessee should remain the well-wisher of the present Raja and of his estate and that she should not commit any such act as might be harmful to him or to his estate. On a breach of this condition the present Raja would not be responsible for the payment of *guzara* to the assessee. These facts point to the conclusion that the title of the present Raja to the estate was considered not free from doubt and I suggest that the payment of maintenance allowance of Rs. 1,000 a month to the assessee in the late Raja's lifetime and of the increased allowance of Rs. 2,500 a month by the present Raja was nothing more than a consideration for the purchase of the assessee's acquiescence in the present Raja's

succession to and holding of the estate and the renouncement of her own rights therein. It is significant that the present Raja executed the deeds increasing the assessee's allowance to Rs. 2,500 a month only fifteen days after the late Raja's death. In any view of the case it is clear that the sum of Rs. 2,500 a month paid to the assessee by the present Raja does not represent the measure of the maintenance allowance which would ordinarily have been payable to her as a widow of the joint family even if in law she could be regarded as such. Apart altogether from the motive of the parties to the agreement it is, I submit, obvious that by this agreement the assessee has secured a contractual right to a fixed annuity in exchange for an indeterminate right under the Hindu law to an uncertain allowance fluctuating with the fortunes of the family. In other words, the amount receivable by the assessee under the agreement has a legal character quite different from that attached to the amount, if any, receivable by her as a member of a Hindu undivided family. The former derives from contract: the latter from status. I, therefore, submit that the allowance of Rs. 2,500 a month was paid to the assessee by the present Raja not as the maintenance to which she was properly entitled as a widow of the joint family but for other considerations.

The answer to the second part of the question should therefore, in my respectful opinion, also be in the negative.

In conclusion I would refer again to the case of *Shrimati Rani Rudh Kumari*¹. In that case the Rani Saheba was entitled to *gusara* of Rs. 3,500 a month under the will of a previous holder of the estate. Actually, however, she received maintenance allowance at the rate of Rs. 2,500 a month only from the Court of Wards which was managing the estate. This led your Lordships to infer that the Rani Saheba had waived her rights under the will and agreed to receive only the smaller amount presumably considered appropriate by the Court of Wards having regard to the extent of the estate and the status of the proprietor; and in these circumstances your Lordships concluded that the allowance of Rs. 2,500 a month received by the Rani Saheba was not referable to the will but was granted to her as maintenance in virtue of her position as the mother of the proprietor. It is clear from the judgment of the Hon'ble Mr. Justice Bennett that the decision turned solely on the difference between the two amounts. In the present case, however, as shown above, the amounts of maintenance allowance received by the assessee were the precise amounts fixed in the deeds of the 30th December, 1932, executed by the present Raja and this shows that the maintenance allowance was received by her in virtue of her rights under those deeds and not by any other right.

(1) (1940) 8 I.T.R. 607.

For the above reasons I submit that your Lordships' answer to both parts of the question of law set out in paragraph 3 above should be in the negative.

6. As required by the prescribed rules, a copy of the final draft of the statement of facts and question of law was sent to the assessee for criticism. In her reply, dated the 11th October, 1941, of which a copy is annexed as Exhibit K, the assessee has intimated through her Advocate that she has no objection to the statement."

S. C. Das, for the Commissioner.

H. D. Chandra, for the assessee.

JUDGMENT.

This is a reference under Section 66 (3) of the Income-tax Act by the Commissioner of Income-tax, consequent on an order passed by this Court on the 28th September, 1939*, directing him to state a case.

The assessee under consideration is Srimathi Rani Anand Kunwar of Lakhimpur. The question of law has been formulated by the Commissioner in these terms :—

"Whether the assessee is a member of a Hindu undivided family within the meaning of Section 14 (1) of the Act; and, if so, whether she received the maintenance allowance in dispute in such capacity?"

Shrimati Rani Anand Kunwar of Lakhimpur is the widow of the late Raja Krishna Dutt Singh, Taluqdar of Oel and Kaimarah estates. The present Raja Yuvraj Dutt Singh is his grandson.

During the lifetime of the late Raja the assessee received an annual allowance for maintenance and other expenses. He died on the 15th December, 1932, and the assessee became entitled under a will executed by him some years previously to a maintenance allowance of Rs. 1,000 a month. But on the 30th December, 1932, the present Raja, who had succeeded his grandfather (his father having predeceased the latter), executed two deeds in favour of the assessee under which she was to receive an allowance of Rs. 2,500 a month as maintenance allowance and Rs. 500 a month as pilgrimage and other expenses. These allowances are the subject of the present reference.

On the assessment for 1933-34 inquiry was made by the Income-tax Officer from the Raja as to whether the assessee and other *guzaradars* were members of his joint family, and the reply being in the negative and the assessee returning her *guzara* income for this and the following year in compliance with the usual notices, assessment was made accordingly upon it.

The assessee appealed to the Assistant Commissioner who dismissed her appeal on the ground that she was not a member of a Hindu

*See (1940) 8 I.T.R. 126.

undivided family. She then applied to the Commissioner, asking him either to cancel the assessment in exercise of his revisional powers, or, in the alternative, to refer certain questions of law to this Court. The application was rejected and the assessee then applied to this Court under Section 66 (3) of the Act.

The order passed by this Court on the 28th September, 1939, shows that the Commissioner had rejected the assessee's prayers on the ground that the assessee should have disputed her liability before the Income-tax Officer, and not having done so she could not thereafter dispute the assessment. This Court did not accept this view.

In directing the Commissioner to state a case this Court observed¹ :—

“It was further argued that for the application of Section 14 (1) of the Indian Income-tax Act two conditions are necessary: the assessee should establish that he is a member of a Hindu undivided family and further that the sum under assessment was received by him as such. In the present case it was contended that there is no evidence that the amount in question was received by the applicant as a member of the Hindu family and so this Court, which is not sitting as a Court of appeal against the order of the Commissioner of Income-tax, should not require the Commissioner to refer a question of law which does not directly arise in the case and which is not decisive of the case. We are not prepared to allow this contention to be raised at this late stage. The assessment of the petitioner has proceeded all along upon the footing that the petitioner received the sum under assessment as a member of a Hindu undivided family, if in law she could be regarded as such. The question whether the income under assessment has been received as a member of the joint Hindu family is dependent upon whether she is such member or not. At no stage of the case it was hinted that she received this money in any other capacity or in recognition of any other right. The only question addressed by the Income-tax Officer to the Taluqdar was whether she was a member of an undivided family or not. He never entertained any doubt as to her receiving the money in the right of a Hindu widow in the family. Further, no such question was raised either before the Court of appeal or before the learned Commissioner of Income-tax, and it is too late to raise that question now.”

It is clear from the above that the only question which arises out of this order is whether the assessee is a member of a Hindu undivided family within the meaning of that term in Section 14 (1), the further question whether she received the allowance in question in this capacity being expressly excluded from consideration.

(1) See (1940) 8 I.T.R. 125 at 131.

The Commissioner of Income-tax has, however, included the latter point in the question formulated by him and the learned Counsel for the department has asked us to consider it, notwithstanding its exclusion by the order of this Court. He contends that the directions and remarks quoted from this order were based on a misapprehension, the contention that the allowances had not been received by the assessee as a member a Hindu undivided family having in fact been raised at the earliest opportunity.

Section 14 (1) provides that "The tax shall not be payable by an assessee in respect of any sum which he receives as a member of a Hindu undivided family" and we are not ourselves clear that it was never definitely accepted by the Income-tax department that the assessee received these allowances as such a member "if in law she could be regarded as such." We understand that since the Raja's reply, their main case has been that she was not a member of a Hindu undivided family and not entitled therefore to exemption. On this view the second part of the question did not arise. The estate is an impartible estate regulated by the Oudh Estates Act and the allowances were presumably granted by the present Raja out of the estate in pursuance of the provisions of Sections 24 and 25 of that Act. These provisions apply alike to Muhammadans and Hindus and it does not follow because an allowance has been given by a Taluqdar to a Hindu widow who would be entitled to an allowance under ordinary Hindu law if she is a member of a Hindu undivided family, that it has been given to her in this capacity. The Commissioner in his order of reference has suggested that the allowance was increased by the present Raja in consideration of the assessee's acquiescence in his succession and cannot therefore be regarded wholly in the light of maintenance, but this aspect of the case has not been referred to in arguments before us and we propose therefore to exclude it from consideration. Otherwise the Commissioner's argument, apart from the question whether the assessee is or is not a member of a Hindu undivided family, is that the amounts receivable by the assessee under the deeds of the 30th December, 1932, have a legal character quite different from that which would attach to an amount receivable by a widow as a member of a Hindu undivided family. A claim based on contract has been substituted for one based on status.

The question whether a person is or is not a member of a Hindu undivided family is primarily a question of fact, as was held by the Allahabad High Court in the case of *Makhan Lal Ram Sarup*¹ and by the Patna High Court in *Commissioner of Income-tax, Bihar and Orissa v. Visheshwar Singh*². So far as the evidence goes we have

(1) (1925) A.I.R. 1925 All. 298.

(2) (1935) 3 I.T.R. 216; A.I.R. 1935 Pat. 342.

merely on the one side the reply of the present Raja to the Income-tax Officer, considered with the admitted fact that the estate is impartible, and on the other, the assessee's claim to be a member of a Hindu undivided family. We have not been referred to any other evidence and we think that it would be difficult to hold upon this evidence that the view taken by the Income-tax authorities was not justified.

As regards the effect on this question of the estate being impartible and held by a single person under the Oudh Estates Act we were referred for the assessee to the case of *Commissioner of Income-tax, Bombay v. Laxminarayan*¹, which shows that a Hindu joint family does not cease to be such on the devolution of the ancestral property by survivorship on a single person. It was held in that case that this person, his mother and his wife continue to be members of a Hindu undivided family for the purpose of income-tax. On the other hand it was held by the Patna High Court in *Commissioner of Income-tax, Bihar and Orissa v. Sir Rajendra Narayan Bhanja Deo of Kanika*², that the income of an impartible estate in the hands of the holder is to be assessed on the footing that the income is the income of an individual and not of an undivided family. This case supports the view taken by the Income-tax department in the present case, although the income of the holder and not the income of a *guzaradar* was under consideration. We were also referred to the decision of this Court in *Commissioner of Income-tax, C.P. and U.P. v. Rudh Kumari*³, to which one of us was a party, as showing what is meant by the expression "Hindu undivided family" in Section 14. It was held that it should not be restricted to members of the coparcenary body. A similar view has been taken by other Courts and it has not been disputed before us but it does not go very far to prove the present assessee's case. The learned Counsel for the Income-tax department relied on the judgment of one of us in that case, as drawing a distinction between an allowance granted purely by way of maintenance on the basis of status and a maintenance allowance based on a will. The question whether any member of a Hindu family is entitled to exemption under Section 14 as a member of a Hindu undivided family, when the estate from which the allowance is paid is impartible, was not considered in that case. Another cognate question which too was not discussed in *Rudh Kumari's case*³, is whether it is implicit in Section 14 that the allowance should come out of joint family funds, a question on which different views have been taken in Madras and the Punjab, vide *Commissioner of*

(1) (1935) I.L.R. 59 Bom. 618; 3 I.T.R. 367.

(2) (1938) 6 I.T.R. 536.

(3) (1940) 8 I.T.R. 607; 1940 O.W.N. 853.

*Income-tax, Madras v. Narayana Gajapathi Raju Bahadur Garu*¹ and *Kunwar Kartar Singh v. Commissioner of Income-tax, Punjab*².

For the purpose of the present reference we think it only necessary to say that we are satisfied that the assessee has failed to prove that she is a member of a Hindu undivided family within the meaning of Section 14 (1) of the Income-tax Act basing this finding on the evidence, such as it is, to which we have referred, and the fact that the estate is not held by a joint Hindu family, but by a single holder under the Oudh Estates Act. We answer the first part of the question referred accordingly, leaving the second part unanswered as not arising. The learned Counsel for the department is entitled to recover his fees which we fix at Rs. 100.

First part of the question answered accordingly.

[IN THE MADRAS HIGH COURT.]

O. Rm. M. SP. S. V. MEYYAPPA CHETTIAR

v.

COMMISSIONER OF INCOME-TAX, MADRAS.

SIR LIONEL LEACH, C. J., and PATANJALI SASTRI, J.

March 12, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922 AFTER AMENDMENT IN 1939), SECS. 25 (3), (5) & 26 (2)—DISCONTINUANCE—WHETHER INCLUDES SUCCESSION—BUSINESS OF JOINT HINDU FAMILY TAXED UNDER 1918 ACT CARRIED ON BY MEMBERS AS PARTNERS FROM 2ND JUNE 1938—WHETHER FAMILY ENTITLED TO THE BENEFIT OF SEC. 25 (3)—CLAIM FOR EXEMPTION FROM TAX—LIMITATION.

Section 25 (3) of the Indian Income-tax Act, 1922, as amended by the Indian Income-tax (Amendment) Act, 1939, which provides for relief where a business charged to tax under the Income-tax Act, 1918, is discontinued does not apply when a Hindu undivided family carrying on business which was taxed under the Act of 1918 becomes disrupted and the members continue the business thereafter as partners. The word "discontinuance" in Section 25 (3) means "cessation" and does not cover cases of succession.

The words "claim to the relief afforded under sub-section (3)" in Section 25 (5) refer only to the relief by way of adjustment of the tax levied on the income of the previous year and the consequential refund, if any, for which the assessee has to make a claim and do not refer to the exemption from tax of the income of the period between the end of

(1) (1934) 2 I.T.R. 288; A.I.R. 1934 Mad. 608.

(2) (1937) 5 I.T.R. 569, at 579.

the previous year and the date of the discontinuance for which the assessee need not make a claim.

A joint Hindu family carried on a money-lending business and this business had been assessed to tax under the Income-tax Act of 1918. On the 2nd June 1938 the family disrupted and the members thereafter continued the business as partners. On the 22nd December 1939 it was claimed that the income of the family from the commencement of the financial year, i.e., 13th April 1938, to 2nd June 1938, was not liable to be taxed by virtue of Section 25 (3) :

Held, that the claim was not barred by limitation but the income of the family from the 13th April 1938 to the 2nd June 1938 was not exempt from tax under Section 25 (3).

P. E. Polson, In re [1942] (I.L.R. 1942 Bom. 216 ; 10 I.T.R. 52) not followed.

Cases referred to :—

Bartlett v. Inland Revenue Commissioners (1914) 3 K.B. 686 ; 84 L.J.K.B. 106 ; 111 L.T. 852 ; 7 Tax Cas. 229.

Commissioner of Income-tax, Bombay v. P. E. Polson (1942) I.L.R. 1942 Bom. 216 ; 10 I.T.R. 52.

Commissioner of Income-tax, Bombay v. Sanjana & Co., Ltd. (1926) I.L.R. 50 Bom. 87 ; A.I.R. 1926 Bom. 129 ; 2 I.T.C. 110.

Commissioner of Income-tax, Madras v. Karuppiiah (1941) 9 I.T.R. 1 ; I.L.R. 1941 Mad. 220 ; 194 I.C. 118 ; 53 L.W. 210 ; 1941 M.W.N. 317 ; A.I.R. 1941 Mad. 255 ; (1941) 1 M.L.J. 120.

Hanutram Bhuramal v. Commissioner of Income-tax, Bihar & Orissa (1938) 6 I.T.R. 290.

Kalu Mal Shori Mal v. Commissioner of Income-tax, Punjab (1929) 3 I.T.C. 341 ; 117 I.C. 228 ; A.I.R. 1929 Lah. 461.

Michael Faraday and Others v. Carter (1927) 11 Tax Cas. 565.

Case referred to the Madras High Court under Section 66 (3) of the Indian Income-tax Act (XI of 1922), in pursuance of the High Court's order dated 20-7-1942 in O. P. No. 86 of 1942, by the Commissioner of Income-tax, Madras, for the decision of the following question :—

“ Whether the income of the family from the 13th April 1938 to the 2nd June 1938 is not liable to be taxed by virtue of Section 25 (3) of the Income-tax Act ? ”

O. P. No. 86 of 1942.

STATEMENT OF CASE.

“ In accordance with the High Court's order quoted above, I have the honour to refer the following case for the decision of the Honourable Judges of the High Court under Section 66 (3) of the Indian Income-tax Act, XI of 1922, before the amendment on 1-4-1939 (hereinafter referred to as the Act).

2. The petitioner and his two brothers were members of a Hindu undivided family within the jurisdiction of the Income-tax Officer, Devakotta. The family derived income from property and carried on

money-lending business at several places both in and outside British India. In the course of the assessment for 1939-40, the year under consideration, it was claimed on 20-6-1939 that the family had become divided as from 20th Vaikasi, Bahudanya (2-6-1938) and that a form of return might be given to the petitioner to enable him to return the income of the period 1st Chitrai to 19th Vaikasi, Bahudanya (13-4-38 to 2-6-38). On 22-12-1939 it was claimed that the income of the above period was not liable to be taxed under Section 25 (3) and (4) of the Act since the family had become disrupted and the members of the family had succeeded to the business of the family. The Income-tax Officer accepted the petitioner's statement regarding partition but refused to accept the claim that the income of the family from 13-4-38 to 2-6-38 was not liable to be taxed under Section 25 (3) and (4). He held that Section 25 (3) did not apply as there was no discontinuance of the businesses, the businesses having been continued by the members of the family, and that Section 25 (4) had no application as the businesses were not carried on by the Hindu undivided family at the commencement of the Indian Income-tax (Amendment) Act, 1939, and therefore did not come under the purview of that section. He accordingly made an assessment on the income of the family in respect of the period 13-4-38 to 2-6-38 on a total income of Rs. 15,531. An extract of the assessment order is filed marked Exhibit A.

3. The petitioner appealed to the Appellate Assistant Commissioner, Trichinopoly, but without success. An extract of his order is filed marked Exhibit B.

4. The petitioner then filed an application under Section 66 (2) of the Act and required my predecessor to refer to the High Court certain questions alleged to be questions of law. My predecessor declined to do so on the ground that no questions of law arose for decision. An extract of his order is filed marked Exhibit C.

5. The petitioner then moved the High Court under Section 66 (3) of the Act and the High Court has by its order dated 20th July 1942 directed me to state a case and refer the following question of law, which I accordingly refer for the decision of the Hon'ble Judges of the High Court :

“Whether the income of the family from the 13th April 1938 to the 2nd June 1938 is not liable to be taxed by virtue of Section 25 (3) of the Income-tax Act?”

6. The petitioner's claim which is based on sub-section (3) of Section 25 is, in the first place, barred by time as under sub-section (5) of the same section no claim to the relief provided in sub-section (3) thereof shall be entertained unless it is made before the expiry of one

year from the date on which the business was discontinued. The application in this case was preferred on 22-12-1939, i.e., more than one year and six months after the date on which the alleged discontinuance took place, namely, 2-6-1938.

7. Apart from this, it has been found by the Income-tax Officer that the business was not, in fact, discontinued. The identical business which was being carried on by the family before disruption continues to be carried on by all the members of the same family, even after its disruption, and in the same manner as before, and there cannot be said to have occurred a discontinuance of the business. This view has been confirmed in a number of High Court judgments. In *Jupudi Kesava Rao's case*¹ there was a family business conducted by a Hindu father and son. The father died and the son carried on the business. Their Lordships in holding that the case was not even one of succession, remarked: "It appears to us that the word 'succession' as used in the section connotes a transfer of ownership and the person who succeeds another must have by such succession become the owner of the business which his predecessor was carrying on and which he after the succession carries on in such capacity, that is, the capacity as owner. If this view is correct, as we think it is, then it seems fairly clear that the undivided Hindu family which was carrying on business has not been 'succeeded' in such capacity by the petitioner as the petitioner was himself in part the owner of the property already and as such there has been no transfer of ownership in the business as he has become entitled to it by survivorship." This case was applied in *Thontepu Chinna Pullaya and Others v. Commissioner of Income-tax, Madras*², in which the facts were nearly similar to those of the present case. A Hindu undivided family carrying on business became divided. After partition the members constituted themselves into a firm and continued the business carried on by the undivided family. Their Lordships applied the principle of *Jupudi Kesava Rao's case*¹ and held that "all the members of the new firm were members of the undivided family and they now have the same share in the business of the firm as they had in the family business at the date of partition. Applying that case (viz., *Jupudi Kesava Rao's case*¹) to this, the answer to the question propounded must be that the assessment must be in accordance with Section 25A (2) of the Income-tax Act." In *Karuppiiah Pillai's case*³ repelling an argument similar to the one advanced in the present case their Lordships held that the word "discontinuance" in Section 44 does not include a case in which a business carried on by two partners was subsequently carried on by one of them. Their Lordships held

(1) (1935) 3 I.T.R. 339. (2) (1937) 5 I.T.R. 132; 9 I.T.C. 377. (3) (1941) 9 I.T.R. 1.

that the case was one not of discontinuance but of succession. The present case is governed by the same principles and does not attract the provisions of Section 25 (3).

8. It is submitted that there has been no change in the scope of Section 25 (3) by the Amendment of 1939. The only change which Section 25 (3) has undergone is the addition of the words "unless there has been a succession....." immediately after the word "discontinued." This is merely to take out of the section certain category of cases which are separately provided for under Section 25 (4). It does not alter or affect in any way the scope of the section or bring within its scope some cases of "succession" as distinguished from cases of "discontinuance."

In *Polson's case*¹ the amended provisions of Section 26 (2) have been relied upon for construing Section 25 (3). It is submitted with great respect that this is not a correct method of interpreting the section. Nor does the reasoning in the said decision justify a departure from the authoritative exposition of the distinction between discontinuance and succession in the cases cited above. The new Section 26 (2) apportions liability for tax between the transferor and the transferee of a business. As a corollary to this, provision for relief in the case of assesseees who were assessed under the 1918 Act had to be made. This was done in Section 25 (4). It does not follow from this that an enlarged meaning can be given to the word "discontinued" in Section 25 (3) or that one should read into it cases of succession in the face of the express construction to the contrary in the decision of the Madras High Court cited above. It may be added that if and when the business is discontinued or succeeded to hereafter by another person the petitioner will be entitled to the relief under Section 25 (3) or (4) as the case may be.

It is further submitted that the word "discontinuance" occurs in Sections 25 (1), 25 (3) and 44. Neither in the first nor in the last of these sections can it be said that it includes succession. There is no reason why a different meaning should be ascribed to it in Section 25 (3). The interpretation of the section before the amendment of 1939 has not been rendered inadequate by the said amendment."

N. Sreenivasa Ayyangar for *V. Ramaswami Aiyar*, for the assessee.

K. V. Sesha Ayyangar and *K. S. Sreenivasan*, for the Commissioner.

JUDGMENT.

LEACH, C.J.—This reference has been made by the Commissioner of Income-tax, Madras, in accordance with a direction given to him

by this Court under Section 66 (3) of the Indian Income-tax Act, 1922. The reference involves the interpretation of Section 25 (3) of the Act.

The petitioner and his brothers were members of an undivided Hindu family, and when joint the family carried on a money-lending business in India and in the Federated Malay States. The business was of long standing and had been assessed to income-tax under the Act of 1918. On the 2nd June 1938 the joint status was severed. Thereafter the members of the family continued the business in the same places as partners. The financial year with which this reference is concerned commenced on the 13th April, 1938. On the 22nd December 1939 the petitioner claimed that the income of the family from the 13th April 1938 to the 2nd June 1938 was not liable to be taxed by reason of the provisions of sub-sections (3) and (4) of Section 25. The Income-tax Officer accepted the petitioner's statement that there had been a partition, but he rejected the contention that the family was not liable to pay the tax on the profits earned between the 13th April and the 2nd June 1938. The petitioner appealed to the Appellate Assistant Commissioner who agreed with the Income-tax Officer. The petitioner then asked the Commissioner to make a reference to the Court under Section 66 (2) and as the Commissioner refused to do so, the petitioner moved the Court for an order under sub-section (3) of that section directing the Commissioner to make a reference. The Court directed the Commissioner to refer for decision the following question :—

“ Whether the income of the family from the 13th April 1938 to the 2nd June 1938 is not liable to be taxed by virtue of Section 25 (3) of the Income-tax Act ? ”

In his statement of the case the Commissioner has suggested that the application of the petitioner made to the Income-tax Officer on the 22nd December, 1939, was out of time, and it is necessary to decide this question as well, because naturally the Court is not prepared to embark upon an academic discussion of the question referred if the petitioner has delayed beyond the period allowed by law in raising his objection. To decide the question of limitation regard must be had to the provisions of sub-section (5) as well as the provisions of sub-section (3) of Section 25. Sub-section (3) reads as follows :—

“ Where any business, profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918, is discontinued, then, unless there has been a succession by virtue of which the provisions of sub-section (4) have been rendered applicable, no tax shall be payable in respect of the income, profits and gains of the period between the end of the previous year and the date of such

discontinuance, and the assessee may further claim that the income, profits and gains of the previous year shall be deemed to have been the income, profits and gains of the said period. Where any such claim is made, an assessment shall be made on the basis of the income, profits and gains of the said period, and if an amount of tax has already been paid in respect of the income, profits and gains of the previous year exceeding the amount payable on the basis of such assessment, a refund shall be given of the difference."

Sub-section (5) states :—

"No claim to the relief afforded under sub-section (3) or sub-section (4) shall be entertained unless it is made before the expiry of one year from the date on which the business, profession or vocation was discontinued or the succession took place, as the case may be."

The Commissioner says that by his application of the 22nd December 1939 the petitioner was claiming "relief" under sub-section (3) and as the application was made more than one year from the date on which the family ceased doing business as a family the sands had run out. On the other hand, the petitioner says that the word "relief" in sub-section (5) has, so far as sub-section (3) is concerned, reference only to the words "and the assessee may further claim that the income, profits and gains of the previous year shall be deemed to have been the income, profits and gains of the said period" which are to be found therein. He points to the fact that sub-section (3) states emphatically that a business on which a tax was charged under the provisions of the Act of 1918 shall not be chargeable in respect of the income of the period between the end of the previous year and the date of discontinuance and he says that "relief" cannot be contemplated in this connection because it must be presumed that the Income-tax Officer will carry out his duties in accordance with the provisions of the Act. Besides being exempt from tax during this period the assessee is allowed to claim a refund if an amount of tax has already been paid in respect of the income of the previous year exceeding the amount payable on the basis of the income received in the year of discontinuance. He is entitled to recover the whole of the difference. It is said that it is here that a provision for relief is necessary and sub-section (5) has been inserted in order to impose a time limit.

In my judgment the petitioner's contentions are sound. The Legislature could only contemplate the Income-tax Officer doing his duty and therefore would not consider it necessary to provide for "relief" against an illegal order. The provisions to be found in the Act with regard to appeal and reference are there for that purpose. Under the Act of 1918 an assessee paid the tax for a particular year

on the income actually earned in that year. The Act of 1922 effected a great change. An assessee now pays the tax in the year of assessment on the income earned in the previous year. Sub-section (3) of Section 25 of the present Act is designed to prevent the injustice of double taxation and in order to do this it is necessary to give the assessee a refund should his income in the year of discontinuance be less than his income for the previous year. It seems to me that it is only in this connection that the word "relief" is used in sub-section (5).

Turning now to the main question, in *Commissioner of Income-tax, Madras v. Karuppiah*¹ this Court held that where a partner carried on the business of the partnership after its dissolution he succeeds to the business within the meaning of Section 26 (2) and can be assessed to tax in respect of the profits of the business for the previous year. This decision applies in the present case and the partnership must be deemed to have succeeded to the business of the family. This is not disputed, but the petitioner says that sub-section (3) of Section 25 stands alone and that the word "discontinued" should not be read as "cessation" of business. Here reliance is placed on the decision of the Bombay High Court in *Commissioner of Income-tax, Bombay v. P. E. Polson*², where this argument was accepted. The Bombay High Court considered that the word "discontinued" by itself, and if not controlled by the context, would cover a discontinuance by disposal.

I find myself unable to share this opinion. In the first place, the same word is used in Section 44 which says that where a business, profession or vocation carried on by a firm or association of persons has been discontinued, or where an association of persons is dissolved, every person who was at the time of discontinuance or dissolution a partner or a member shall, in respect of the income, profits and gains of the firm or association, be jointly and severally liable to assessment under Chapter IV and for the amount of tax payable. This section clearly deals with a case of cessation of business. The word "discontinued" in sub-section (3) of Section 25 cannot be given a different meaning from the meaning it has in Section 44 unless the context in sub-section (3) demands it, and I can find nothing in sub-section (3) which would warrant the Court departing from this well accepted rule of construction. On the other hand, I consider that the words "then, unless there has been a succession by virtue of which the provisions of sub-section (4) have been rendered applicable" which follow the word "discontinued" in Section 25 (3) give strong indication that the word "discontinued" there means "cessation." As already pointed

(1) (1941) I.L.R. 1941 Mad. 220 ; 9 I.T.R. 1. (2) (1942) I.L.R. 1942 Bom. 216 ; 10 I.T.R. 52.

out, sub-section (3) has been inserted merely for the purpose of preventing double taxation.

Full support for this opinion is to be found in the judgment of Scrutton, J., in *Bartlett v. Inland Revenue Commissioners*¹, where it was held that if the owner of a business sells it to a company, the business is not discontinued within the meaning of Section 24 (3) of the Finance Act, 1907, which provides that where a profession, trade, or vocation is discontinued, a person charged or chargeable with income-tax in respect of that profession, trade or vocation shall be chargeable on the actual amount of the profits or gains arising from the profession, trade or vocation in that year. It was there argued that the appellant's trade having been discontinued in the year, he was only chargeable on the actual amount made in that year, and there was no power to go back to three years' average. In dealing with this contention Scrutton, J., said:—"The answer to that appears to me to be very simple. The trade was not discontinued in the year. The trade was sold to a company and continued during the whole year." In the present case the business was continued by the same persons, not as members of a joint family, but as partners.

For these reasons, I hold that the income of the family from the 13th April 1938 to the 2nd June 1938 is liable to be taxed by virtue of Section 25 (3), and I answer the reference accordingly. The Commissioner is entitled to his costs, which I would fix at Rs. 250.

PATANJALI SASTRI, J.—I agree that the reference should be answered as suggested in the judgment just delivered by my Lord. In view, however, of the different opinion expressed by the Bombay High Court in *P. E. Polson, In re*², which was strongly pressed upon us by the assessee's learned counsel, I wish to add a few observations.

The question is whether Section 25 (3) of the Indian Income-tax Act, 1922, as amended by the Indian Income-tax (Amendment) Act, 1939, providing for certain reliefs in cases of discontinued business etc., charged to tax under the Indian Income-tax Act, 1918, applies when a Hindu undivided family carrying on business becomes disrupted and the members continue the business thereafter as partners; in other words, does the discontinuance which the provision has in view refer only to the closing down or extinguishment of a business etc., or cover succession to a business which is continuing. The question of discontinuance or succession was of special importance in England in view of the basis of taxation being different in either case

(1) (1914) 3 K.B. 686; 7 Tax Cas. 229.

(2) (1942) 10 I.T.R. 52.

(Vide Rules 8 (2) and 11 of the Rules applicable to Cases I and II, Schedule D, of the Income Tax Act, 1918) and the terms have acquired well recognised meanings in income-tax usage. (See *Bartlett v. Commissioners of Inland Revenue*¹, *M. Faraday and Others v. Carter*².) They have accordingly been adopted in the Indian Income-tax Act, 1922, as denoting two different situations for which the Act makes separate provisions in Sections 25 and 26, and before the Amendment Act of 1939 was passed the Courts in this country, including the Bombay High Court had uniformly held that "discontinuance" for the purpose of Section 25 did not cover mere change of ownership. (See *Commissioner of Income-tax, Bombay v. Sanjana & Co., Ltd.*³, *Kalu Mal Shori Mal v. Commissioner of Income-tax, Punjab*⁴, *Hanu-tram Bhuramal v. Commissioner of Income-tax, Bihar & Orissa*⁵.) But it is argued—and the argument was accepted by the Bombay High Court in the case already referred to—that the amendments introduced in Sections 25 and 26 by the Act of 1939 now compel a different interpretation of the term in Section 25 (3). It seems to me, however, with all respect, that the well-marked distinction for purposes of assessment between discontinuance and succession has not been obliterated by the recent amendments and that it would lead to considerable confusion in working the Act if the provisions specifically relating to the one were understood as applicable to the other. For instance, Section 25 (1) provides for an accelerated assessment when a business etc., which was not at any time charged under the Act of 1918 is "discontinued," evidently as a safeguard against risk to Revenue which the delay in assessing a person who is no longer in business involves as such person might disappear or become insolvent before the normal time for assessment arrives. Now if "discontinuance" is to be understood as covering change of ownership—the word must obviously have the same meaning in both sub-section (1) and sub-section (3)—the the special procedure indicated in Section 25 (1) would become applicable to cases of succession, for which, however, specific provision is made in Section 26 (2) for an apportioned assessment in the normal course, i.e., in the year following the succession, with different safeguards for the protection of Revenue in the contingencies aforementioned. This would result in an incoherent scheme of assessment.

Turning now to the amendments introduced by the Act of 1939 on which the assessee's learned counsel relies in support of his contention, it is true that Section 26 (2) has been amended so as to provide,

(1) (1914) 3 K.B. 686; 7 Tax Cas. 229.

(2) (1927) 11 Tax Cas. 565.

(3) (1926) I.L.R. 50 Bom. 87.

(4) (1929) 3 I.T.C. 341.

(5) (1938) 6 I.T.R. 290.

in the case of a succession in business etc., for the assessment of the predecessor and the successor each in respect of his actual share of the profits of the previous year, instead of, as before, assessing the successor in respect of the profits earned even by the predecessor. The predecessor having thus been made liable for tax in respect of his share of profits in the year of succession, it is only fair that he should be relieved from this burden, in cases where his business etc., had been charged under the Act of 1918, for precisely the same reason as in the case of discontinuance of a business etc., so charged, *viz.*, to redress the hardship involved in the assessment of the profits of the year 1921-22 twice over, once in that year as the income thereof on adjustment under the Act of 1918, and once in the next year as the income of the previous year under the Act of 1922. Hence the enactment of the new sub-section (4) of Section 25 extending the benefit conferred under Section 25 (3) to cases of succession to a business, profession etc., charged under the Act of 1918. This provision, however would make it possible for the relief in respect of the double assessment referred to above being claimed more than once if the change of ownership occurred after 1st April 1939, once by the predecessor at the time of succession and once by the successor when the latter closes down the business in any subsequent year. This had to be provided against, as such relief has to be granted only once and that to the predecessor who suffered the double assessment, and Section 25 (3) was accordingly amended so as to exclude the successor from its benefits when he discontinues the business subsequently as, so far as he is concerned, he will have suffered tax only for the exact number of years for which he has carried on the business. Hence the insertion of the words "then unless there has been a succession by virtue of which the provisions of sub-section (4) have been rendered applicable" after the word 'discontinued' in sub-section (3). The learned Judges in *P. E. Polson, In re*¹, apparently thought that this exception applied only where succession and subsequent discontinuance both occurred in the same year as they referred to it as contemplating a case "very unlikely to occur but at the same time possible." But the exception clearly covers a wider ground and operates to exclude the successor from the benefits of the sub-section whenever he may discontinue the business.

Such being the objects and reasons of the relevant amendments introduced in 1939, I find it difficult, with all respect, to see why they should be regarded as having the effect of widening the scope of the term 'discontinuance' in Section 25 (3) so as to cover cases of succession. It is true that after the amendments the predecessor in the case

of a change of ownership is put on the same footing as if he had closed down his business on the date of succession for purposes of relief in respect of the double assessment of the profits of 1921-22. But this is done by enacting the new sub-section (4) of Section 25 which provides such reliefs subject to the condition that the predecessor is one who was carrying on the business, profession etc., at the commencement of the Amendment Act. To ignore this condition and to bring the case of a succession occurring before the commencement of that Act within the purview of Section 25 (3) as covered by the word 'discontinued' seems to me opposed alike to sound canons of construction and to the scheme of assessment laid down in the principal Act. It must be remembered that in England a provision for apportionment of the tax burden between the predecessor and the successor in cases of succession (Rule 9 of the rules applicable to Cases I and II, Schedule D, of the Income-tax Act, 1918, corresponding to Section 2, Taxes Management Act, 1880) has been in existence side by side with a provision for relief in cases of discontinuance [Rule 8 (2) of the same rules corresponding to Section 25 (3), Finance Act, 1907], but this has not been considered to warrant the wider interpretation of the word 'discontinued' favoured by the Bombay High Court (see *Bartlett v. Commissioners of Inland Revenue*¹ and *M. Faraday and others v. Carter*² already referred to).

The question of limitation raised by the Commissioner of Income-tax turns on the proper interpretation of the newly introduced sub-section (5) of Section 25 which provides—

“that no claim to the relief afforded by sub-section (3) or sub-section (4) shall be entertained unless it is made before the expiry of one year from the date from which the business, profession or vocation was discontinued or the succession took place as the case may be.”

It will be seen that sub-sections (3) and (4) of Section 25, provide for two concessions in respect of a business, etc., charged under the Act of 1918, namely, (1) an exemption from tax of the income of the period between the end of the previous year and the date of the discontinuance or succession and (2) an adjustment, at the option of the assessee, of the tax levied on the income of the previous year with reference to the profits of the said period and a refund of the excess tax if any, already collected. In the present case the petition sought only concession (1). To obtain that concession the assessee does not have to call upon the Income-tax Officer to do anything. The Act exempts the income of the period in question and the Officer has merely to take note of the exemption and abstain from assessing such income ;

(1) (1914) 3 K.B. 686; 7 Tax Cas. 229.

(2) (1927) 11 Tax Cas. 565.

while for concession (2) the assessee has to make a 'claim' before the Officer, as it involves the Officer doing something, namely, an assessment of the income of the said period and adjustment of the tax paid on the income of the previous year with reference to the income so assessed and a refund of the excess tax, if any, already paid. If the Income-tax Officer has to take action in this manner for granting this relief, it stands to reason that a time limit should be imposed for a claim to be made in that behalf, as the task of making a proper assessment for the relevant period might become increasingly difficult with the lapse of time. But what reason could there be for imposing a time limit for asking the Income-tax authorities to abstain from doing a thing which the Act directs them not to do? A time limit for this purpose would, indeed, mean that the Income-tax authorities would be free to disregard the plain duty imposed on them by the Act, leaving the assessee without a remedy, if only they assess and levy the tax on the exempted profits, either under Section 23 or Section 34, after the expiry of the time limited. It seems to me that a construction of Section 25 (5) which leads to such anomalous results ought not to be readily accepted. It is said that the word "relief" is wide enough to cover both the benefits afforded under sub-sections (3) and (4). It may be so in ordinary usage uncontrolled by context, though the assessee may well retort that not much *relief* is afforded to him when the Crown, having already taxed him for as many years as he carried on the business, merely abstains from taxing once more. But in the context of Section 25 I am of opinion that it would be a reasonable construction of the words "claim to the relief afforded under sub-section (3) or sub-section (4)" to hold that they refer only to the relief by way of adjustment of the tax levied on the income of previous year and the consequential refund, if any, for which the assessee has to make a 'claim' under sub-sections (3) and (4). The plea of limitation cannot therefore prevail. I concur also in the order for costs.

Reference answered accordingly.

[IN THE NAGPUR HIGH COURT.]

MOHAN LAL HIRA LAL

v.

COMMISSIONER OF INCOME-TAX, C. P. AND U. P.

Niyogi and Digby, JJ.

January 18, 1948.

INDIAN INCOME-TAX ACT (XI OF 1922 AS AMENDED IN 1939), SECS.
4 (1) PROVISIO (3), 23 (1), (3), (4), 5 (a)—FOREIGN INCOME—REGISTERED

FIRM—EXEMPTION OF RS. 4,500—WHETHER SHOULD BE ALLOWED FROM TOTAL INCOME OF FIRM OR THE SHARE OF INCOME OF EACH PARTNER.

Where the assessee is a registered firm whose total income includes income accruing or arising without British India, the statutory deduction of Rs. 4,500 allowed by the third proviso to Section 4 (1) of the Income-tax Act should be made when the total assessable income of the firm is calculated and not from each partner's share of income when the tax is levied under Section 23 (5) (a).

The liability of the partners to pay income-tax arises after the total income of the firm is assessed and Section 4 is concerned with the assessment and not with the levy of income-tax.

Case referred to the Nagpur High Court under Section 66 (1) of the Indian Income-tax Act, 1922, as amended by Section 91 of the Indian Income-tax (Amendment) Act (VII of 1939), by the Income-tax Appellate Tribunal, Bombay Bench, for the decision of the following question :—

“ Whether on the facts of the case the applicant was entitled, under proviso 3 to Section 4 (1) of the Indian Income-tax Act, to deduct Rs. 4,500 from his share of the income in the firm included in his own total income in conformity with Section 23 (5) (a) of the Act.”

Miscellaneous Civil Case No. 131 of 1942. The facts of the case appear in the Statement of Case of the Appellate Tribunal.

The appeal to the Appellate Tribunal being unsuccessful, the assessee put in an application under Section 66 (1) of the Indian Income-tax Act (XI of 1922) and the Appellate Tribunal (Bombay Bench) referred the case to the Nagpur High Court on 31st July 1942 :—

STATEMENT OF CASE.

“ We are respectfully making this reference at the instance of the assessee, Mr. Mohanlal Hiralal, Kamptee, Nagpur, under Section 66 (1) of the Indian Income-tax (Amendment) Act, 1922.

2. In his application, marked Exhibit A in the appended list, the applicant has raised only one question as arising out of our appellate judgment in Regular Assessment Appeal No. 42 (C. P.) of 1941-42. In his written answer, Exhibit B, the Commissioner of Income-tax, C. P. and U. P. admits that the question of law does arise.

3. The reference arises out of an assessment to income-tax and super-tax made upon the assessee, for the charge year 1940-41. Up to a certain point, the assessment is closely allied to another made upon the firm of Messrs. Nainsukh Kaniram, Kamptee, Nagpur, of which the applicant is a partner, for the charge year in question. Messrs. Nainsukh Kaniram is a resident firm having its principal seat of business at Kamptee, in British India. It has several branches one of which is at

Rajnandgaon, in an Indian State. In the financial year in question, an assessment was made upon the firm on a total income of Rs. 51,090, which included an amount of Rs. 5,097 as the assessable income of the foreign branch at Rajnandgaon. In working out the latter, the Income-tax Officer made the statutory deduction of Rs. 4,500 from the total income of the branch, as required by the third proviso to Section 4 (1) of the Indian Income-tax Act. The firm had been registered for income-tax purposes. Therefore, instead of determining the tax payable upon the total income of the firm, the Income-tax Officer carried the share of each partner in the firm's income to his individual assessment, in accordance with the provisions of Section 23 (5) (a) of the Act. In this manner, the present applicant assessee was assessed on a total income of Rs. 39,954, which included an amount of Rs. 36,040 representing his share in the firm's assessable income. Copies of the orders of assessment of the firm and the applicant Mr. Mohanlal are, respectively, Exhibits C and D.

4. Both the firm and the applicant Mr. Mohanlal took successive appeals to the Appellate Assistant Commissioner and the Appellate Tribunal. But we are concerned with the point raised in the applicant's case alone. Here it may be mentioned that we disposed of the firm's and the applicant's appeals in one judgment. Copies of the Appellate Assistant Commissioner's order and our judgment are, respectively, Exhibits E and F.

5. The only point raised in the applicant's appeal, and which occasions the present reference, was whether the applicant was entitled to the statutory deduction of Rs. 4,500 from his share of the profits included in his individual assessment. We have stated before that in computing the total income of the firm, the Income-tax Officer made the statutory deduction of Rs. 4,500 out of the total income of the Rajnandgaon branch under the third proviso to Section 4 (1) of the Act. It was contended before us that this was wrong, and that the Income-tax Officer should have made a deduction from each partner's share of the profits. In other words, the contention was that each of the individual partners, and not the firm, was entitled to the statutory deduction. We dismissed it for reasons recorded in paragraph 3* of our judgment. Briefly speaking, we held that it is only the firm that can be allowed the statutory deduction in the computation of its income, and that a partner was not entitled to ask for a deduction from his share of the profits taken on his individual assessment.

6. In this connection, we respectfully invite their Lordships' attention to a judgment of the Calcutta High Court in *In the matter of*

* Para 3 is printed at p. 262 infra.

Babu Raman Lal Kondai, decided on 20th February, 1941, and in particular, to the judgment of Panckridge, J. The case is not reported, and we are appending a copy of the judgment to this reference as Exhibit G.* A very similar contention was made in that case and was repelled by their Lordships.

7. The question formulated by the assessee lacks precision. We therefore respectfully submit the question to their Lordships in the following manner :—

Question Referred.

Whether on the facts of the case the applicant was entitled, under proviso 3 to Section 4 (1) of the Indian Income-tax Act, to deduct Rs. 4,500 from his share of the income in the firm included in his own total income in conformity with Section 23 (5) (a) of the Act.

JUDGMENT OF APPELLATE TRIBUNAL (Para. 3).

Paragraph 3 of the Judgment of the Appellate Tribunal referred to in the Statement of Case is as follows :—

“ 3. It is contended in the first place that the income from Rajnandgaon branch was divided by the partners at that place and became the income of the partners, and that, therefore, it should not have been included in the income of the firm but in the total income of the individual partners. The learned Advocate for the appellant explained the meaning of this contention saying that no statutory deduction of Rs. 4,500 should have been made from the foreign income because it was divided at Rajnandgaon, and became the income of the partners, who, thereafter brought it in British India. In other words, his contention is that instead of making a statutory deduction from the total foreign income of the firm, such a deduction should be made from the share of each partner brought into British India, so that each of the partners may have the benefit of a deduction of Rs. 4,500. This is indeed a startling proposition. In the first place, the firm doing business at Rajnandgaon is not a separate entity but only a branch of the main firm at Kamptee. Next, if we consider the scheme of assessment under Section 23 of the Income-tax Act it will appear that the computation of the income of a firm is to be made just as in the case of an individual assessee up to the stage of working out the total assessable income. It is only after that is done that a direct assessment becomes permissible in the case of a registered firm upon the shares of each partner as provided by Section 23 (5) (a) of the Act. That is to say, it is only at the moment of imposing the tax that a direct assessment is made upon the partners. There is nothing in the Income-tax Act to

* Printed *infra* at p. 263.

support the view that the statutory deduction allowed by the third proviso to Section 4 should be made when levying the tax in the manner laid down by Section 23 (5) (a). On the contrary, the deduction is to be made from the total foreign income before the net assessable income is ascertained. That was exactly what was done in the present case. Acceptance of the appellant's arguments would mean a deduction of Rs. 4,500 in the case of each of the two partners, a course which is certainly not permitted by the Income-tax Act."

The judgment of the Calcutta High Court in *In the matter of Babu Raman Lal Kondai*, referred to in the Statement of Case of the Appellate Tribunal, runs as follows. The judgment was delivered by the Court consisting of Derbyshire, C. J., and Panckridge, J., on the 20th February, 1941.

"DERBYSHIRE, C. J.:—The facts of this Reference are set out in the case stated. The question is "whether in the facts and circumstances of this case the Income-tax Officer was correct in law in holding that the petitioner's income was 6/16ths of Rs. 25,675."

The Commissioner has given his reasons which simply quote in paraphrase the relevant sections of the Income-tax Act. In my opinion the question asked of us can only be answered as the Commissioner has answered it, that is to say, the Income-tax Officer was correct in holding that the petitioner's income was 6/16ths of Rs. 25,675.

PANCKRIDGE, J.—I agree. The assessee has been forced to admit that he cannot claim to exclude the sum of Rs. 4,500 both from the assessment of the firm, and from his own assessment, and he suggests that the Income-tax Officer, should not have excluded that sum from the assessment of the firm, but should have excluded it from the assessment of each individual partner.

In my opinion the Income-tax Officer had no choice but to make the assessment of the firm and ascertain its total income in accordance with Section 4 and had no jurisdiction to abstain from making the deduction of Rs. 4,500 to which the firm was entitled.

That being so, in my opinion, Section 23 (5) means that the share of the income, profits and gains of a firm for the previous year should be included in the total income of each partner, such income, profits and gains having been computed in accordance with Section 4 or, in other words, I do not think it is possible to apply the proviso to so much of a partner's income as represents the share of profits and gains of a firm whose total income has already been ascertained in accordance with Section 4.

I therefore agree with the order that has been made."

J. M. Thakar, for the assessee.

B. B. D. N. Choudhury, for the Commissioner.

JUDGMENT.

This case arises on a reference made by the Income-tax Appellate Tribunal, Bombay Bench, under Section 66 (1) of the Income-tax (Amendment) Act (VII of 1939).^{*} The question which has been submitted to this Court is as follows :—

Whether on the facts of the case the applicant was entitled, under proviso 3 to Section 4 (1) of the Indian Income-tax Act, to deduct Rs. 4,500 from his share of the income in the firm included in his own total income in conformity with Section 23 (5) (a) of the Act.

2. The non-applicant, Mohanlal Hiralal, is a partner of the firm of Nainsukh Kaniram which has its head office at Kamptee in British India. Among its several branches there is one at Rajnandgaon in an Indian State. It is not disputed that the whole firm is one entity carrying on business at different places. The Income-tax Officer, Nagpur, assessed the firm on a total income of Rs. 51,090 including in it the income of the Rajnandgaon branch as well as the rest of the branches. In computing the income of the foreign branch, he made the statutory deduction of Rs. 4,500 in accordance with the third proviso to Section 4 (1) of the Income-tax Act and determined the net assessable income to be Rs. 5,097. The non-applicant's contention was that instead of making a statutory deduction from the total foreign income of the firm such a deduction should be made from the share of each partner so that each of the partners may have the benefit of a deduction of Rs. 4,500. The Appellate Tribunal rejected the contention on the ground that the computation of the income of the firm is to be made just as in the case of an individual assessee up to the stage of working out the total assessable income and that it was only after that was done that a direct assessment becomes permissible in the case of a registered firm upon the shares of each partner as provided by Section 23 (5) (a) of the Act and consequently that the statutory deduction should be made when the total assessable income of the firm is calculated and not when the tax is levied upon each of the partners.

3. After having heard the parties at some length we have come to the conclusion that the view taken by the Appellate Tribunal is right. Section 23 of the Income-tax Act sets out the mode of assessment. As a general rule applicable to all classes of assesseees the Income-tax Officer is required to assess the total income of the assessee and to determine the sum payable by him on the basis of such return ; see

^{*} The reference is evidently to Sec. 66 (1) of the Act of 1922,

Section 23, sub-sections (1), (3) and (4). That is so when the assessee is the person who is charged with the income-tax. But an exception is made in clause 5 (a) of Section 23 in the case of a registered firm. The relevant part of the section runs as follows:—

“Notwithstanding anything contained in the foregoing sub-sections, when the assessee is a firm and the total income of the firm has been assessed under sub-section (1), sub-section (3) or sub-section (4), as the case may be,—

(a) in the case of a registered firm, the sum payable by the firm itself shall not be determined but the total income of each partner of the firm, including therein his share of its income, profits and gains of the previous year, shall be assessed and the sum payable by him on the basis of such assessment shall be determined.”

That enactment clearly contemplates two kinds of assessments :

(1) The assessment of the total income of the firm,

(2) the assessment of the total income of each partner of the firm.

It is clear that the total income of the firm, which has been assessed enters into the calculation of the total income of each partner of the firm. Section 4 (1) (b) (ii) of the Income-tax Act says that the total income of any person includes all incomes, profits and gains from whatever source derived which *inter alia* accrue or arise to him without British India during such year and further the third proviso to Section 4 (1) says “that if in any year the amount of income accruing or arising without British India exceeds the amount brought into British India in that year, there shall not be included in the assessment of the income of that year so much of such excess as does not exceed four thousand five hundred rupees.”

4. The crucial question is whose total income has to be assessed, whether the income of the firm or that of the partner? The total income of a partner, who has other sources of income besides his partnership in the firm, stands on quite a different footing and is independent of the total income of the firm; that income when assessed represents only one of the several sources of the partner's income. In fact the income-tax that is levied on the partner is not levied on his share of the total income of the firm assessed but on his total income derived from all sources. Consequently it would be clear that the direct assessment of the partner's income does not enter at all into the calculation of total income of the firm. The income accruing or arising out of British India accrues directly to the firm and not the partner. The liability of the partners to pay income-tax arises after the total income of the firm is assessed and Section 4 is concerned with the assessment and not with the levy of the income-tax. It must therefore follow

that the statutory deduction of Rs. 4,500 allowed by the third proviso to Section 4 (1) must relate to the assessment of the total income of the firm. The income of the Rajnandgaon shop would be primarily or directly the income of the firm and therefore it would enter into the calculation of the total income of the firm.

5. On behalf of the non-applicant reliance is placed on Section 3 of the Income-tax Act and it is argued that inasmuch as the income-tax is charged on the partner his share of the income of the firm could alone form the basis of the assessment. Section 3 refers, no doubt, to the total income of the partners of the firm but it also speaks of the total income of a firm. The ingredients of the total income are specified in Section 4 and the mode of ascertaining it is laid down in Section 23 of the Income-tax Act. It cannot be overlooked that both Sections 3 and 4 say that they have to be read "subject to the provisions of this Act" which includes Section 23 of the Act. Sections 3 and 4, when so read qualified by Section 23, furnish a conclusive answer to the non-applicant's argument.

6. We answer the question referred to us in the negative.

7. The non-applicant will pay the costs of the applicant. Counsel's fee Rs. 50.

Reference answered in the negative.

[IN THE NAGPUR HIGH COURT.]

CENTRAL INDIA SPINNING, WEAVING
AND MANUFACTURING CO., LTD.

v.

COMMISSIONER OF INCOME-TAX, C. P. AND U. P.

NIYOGI and DIGBY, JJ.

January 25, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE AMENDMENT IN 1939), SEC. 10 (2) (ix)—BUSINESS EXPENDITURE—LITIGATION EXPENSES—EXPENSES INCURRED IN SUIT TO RESTRAIN ANOTHER COMPANY FROM USING SAME TRADE MARK—WHETHER ALLOWABLE DEDUCTION.

The assessee company incurred in the year of account a certain expenditure as legal expenses in connection with a suit which they had brought against another company to restrain the latter from using a trade mark to which the assessee had acquired exclusive right by long user.

Held, that the expenditure was revenue expenditure and was allowable in computing the taxable income of the assessee company from the business.

The word "solely" in Section 10 (2) (ix) is related to the object of expenditure, the earning of profits and gains, and not to the profits and gains of the particular year in which the expenditure is made and deducted.

Case law discussed.

Cases referred to :—

British Insulated and Helsby Cables Ltd. v. Atherton (1924) 10 Tax Cas. 155 ; [1926] A.C. 205 ; 95 L.J.K.B. 336 ; 134 L.T. 289 ; 42 T.L.R. 228.

* Commissioner of Income-tax, C. P. & U. P. v. Messrs. Motiram Nandram (1940) I.L.R. 1940 Nag. 341 ; 8 I.T.R. 132 ; 67 I.A. 71 ; 186 I.C. 54 ; 51 L.W. 129 ; 44 C.W.N. 373 ; 42 Bom. L.R. 323 ; A.I.R. 1940 P.C. 33 ; (1940) 1 M.L.J. 180.

Income-tax Commissioner v. Kameshwar Singh (1940) 8 I.T.R. 52 ; A.I.R. 1941 Pat. 197 affirmed on appeal to P.C. (1942) 10 I.T.R. 214 ; A.I.R. 1942 P.C. 11.

Kangra Valley Slate Co., Ltd. v. Commissioner of Income-tax, Punjab (1935) 3 I.T.R. 324 ; I.L.R. 16 Lah. 479 ; 7 I.T.C. 373.

Magniram Bangor, *In re* (1941) 9 I.T.R. 573 ; I.L.R. [1941] 1 Cal. 572 ; 46 C.W.N. 6.

B. W. Noble Ltd. v. Mitchell (1927) 11 Tax Cas. 372 ; [1927] 1 K.B. 719 ; 96 L.J.K.B. 484 ; 137 L.T. 33.

Onnsworth v. Vickers Limited [1915] 3 K.B. 267 ; 84 L.J.K.B. 2036 ; 113 L.T. 865 ; 6 Tax Cas. 671.

Rhodesia Railways v. Income-tax Collector, Bechuanaland [1933] A.C. 368 ; 2 I.T.R. 442 ; 102 L.J.P.C. 62 ; 149 L.T. 1.

Southern v. Borax Consolidated, Ltd. (1942) 10 I.T.R. Suppl. 1 ; (1940) 4 All E.R. 412 ; [1941] 1 K.B. 111 ; 85 S.J. 94.

Vallambrosa Rubber Co., Ltd. v. Farmer (1910) 5 Tax Cas. 529 ; 1910 Sess. Cas. 519 ; 47 S.C.L.R. 488.

Ward and Company v. Commissioner of Taxes [1923] A.C. 145.

Cases referred to the Nagpur High Court by the Income-tax Appellate Tribunal, Bombay Bench, under Section 66 (1) of the Indian Income-tax Act, 1922 (XI of 1922), as amended by Section 92 of the Indian Income-tax (Amendment) Act, 1939 (VII of 1939), for the decision of the following question :—

"Whether on the facts of the case the legal expense of Rs. 2,577 is a revenue expenditure and a proper deduction in computing the taxable income of the assessee company from business ?"

Miscellaneous Civil Case No. 117 of 1942. The facts of the case appear in the judgment of the Appellate Tribunal.

JUDGMENT OF APPELLATE TRIBUNAL.

Under Section 38 of the Indian Income-tax Act (XI of 1922) the Income-tax Appellate Tribunal, Bombay Bench, consisting of N. R. GUNDIL (Judicial Member) and P. C. MALHOTRA (Accountant Member) delivered the following Judgment on 15th January 1942.

These two appeals are taken by the Central India Spinning, Weaving and Manufacturing Company, Limited, Nagpur, known as the Empress Mills, and relate to its assessments for the years 1938-39 and 1939-40, respectively. The contest before us in appeal No. 11 (relating to the assessment of 1938-39) is in regard to two sums of Rs. 2,577 and Rs. 8,000; and that in appeal No. 12 (relating to the assessment of 1939-40) is in regard to only one item of Rs. 8,000. Both the appeals involve mostly common facts and may therefore be conveniently disposed of in one judgment.

2. The facts material to the first item of Rs. 2,577 are briefly these. The appellant company manufactures dhoties and shirtings which it brands with its particular trade mark called "Nag Chhap" to which it has acquired an exclusive right by long user. In 1933, the Binod Mills Limited, Ujjain, which manufactures similar goods began to brand them with a colourable imitation of the appellant's trade mark. The appellant company brought a suit against the latter complaining of infringement of its trade mark, and obtained a decree on October 3, 1936, restraining the defendant company from making use of the appellant's trade mark or its imitation. In this litigation the appellant company incurred a legal expense of Rs. 2,577 which it sought to deduct from its income in the assessment year 1938-39. The Income-tax Officer, Nagpur, rejected the claim and added the amount to the appellant's income without giving any particular reasons for doing so. In appeal, the Appellate Assistant Commissioner held that the expenditure was incurred to protect the appellant's exclusive right to use the trade mark which, he said, was one of the valuable assets of the appellant company. In other words, he held that the expenditure was in the nature of capital expenditure and upheld the Income-tax Officer's order.

3. The facts bearing on the appellant's claim to deduction of Rs. 8,000 in each of the two assessment years are common. The appellant company has made a Scheme for the benefit of its employees, with the object of keeping them in a state of efficiency and contentment. This is known as the Welfare Scheme. For that purpose the company took a large piece of land on lease from Government in 1925 on payment of a premium of Rs. 69,608. It has built on it a hospital, a school for its employees' children and a number of tenements for the employees, besides providing facilities for sport and recreation. This is called the Bezon Bagh Settlement after the company's late manager Sir Bezonji Mehta. The appellant company bears the cost, or almost the whole of the cost, of maintaining the Settlement, and on this account it claimed a deduction of an expenditure of Rs. 45,973

in the assessment of 1938-39, and Rs. 43,626 in that of 1939-40. In each case, the Income-tax Officer allowed a greater part of the claim disallowing Rs. 8,000 in each year, on the ground that this part of the expenditure could not be deemed to have been incurred solely for the benefit of the company's employees. His view was accepted by the Appellate Assistant Commissioner.

4. Taking up the first item of Rs. 2,577 the appellant's claim is based on Section 10 (2) (ix) of the Income-tax Act, 1922. This clause has since been amended and now occurs as clause (xii) of Section 10 (2) of the Act. But we are not concerned with the amended provision, inasmuch as this case is governed by the old clause which was in force in the assessment year under reference. It is contended on behalf of the appellant company that the civil suit against the Binod Mills Limited, was necessitated by their infringement of the appellant's trade mark, and that therefore the legal expense was incurred for arresting losses or reduction of profits which might have resulted in the goods of the Binod Mills Limited, being accepted as those of the assessee company. This is the substance of the argument made by the learned Advocate for the appellant. As far as we can see, all that it means is that the expenditure incurred by the appellant company was directly connected with its trade and was incurred for the purpose of preventing their profits from being reduced by the illegal use of its trade mark by another company. But the mere fact that an expenditure is incurred in course of trade or that it is even connected with it can be no ground to claim it as a deduction under Section 10 (2) (ix) of the Income-tax Act. The clause makes it perfectly clear that only such expenditure, not being in the nature of capital expenditure, that is incurred for the purpose of earning profits and gains is allowable. Therefore the point really is whether the legal expense claimed in this case was or was not in the nature of capital expenditure. What is or what is not a capital expenditure is, in the main, a question of fact, and must be decided with reference to the circumstances of each case. As remarked by their Lordships of the Privy Council in *The Indian Radio and Cable Communications Company Ltd. v. Commissioner of Income-tax, Bombay Presidency & Aden*¹, it is impossible to formulate a test which will always suffice to discriminate between the expenditure which is and which is not allowable for the purpose of income-tax.

5. The learned Advocate for the appellant cited two cases in support of his contention : *Commissioner of Income-tax, Bihar & Orissa v. Maharajadhiraja Sir Kameshwar Singh of Darbhanga*² and *G. Scammell and Nephew, Ltd. v. Rowles*³. In the *Darbhanga case*², the legal

(1) (1937) 5 I.T.R. 270.

(2) (1940) 8 I.T.R. 52.

(3) (1940) 8 I.T.R. Suppl. 41.

expense that was claimed had been incurred for defending a suit brought against the assessee's father, who was a money-lender, by the shareholders of the United Agra Mills Ltd., claiming damages for the breach of an alleged agreement made by the assessee's father to take over the management and finance the mills. In other words, the plaintiffs complained that the assessee's father had failed to supply a large sum of money. Their Lordships of the Patna High Court held that the deduction was admissible under Section 10 (2) (ix) of the Income-tax Act, remarking that the money which a banker or a money-lender employs in his business is his stock-in-trade, and that therefore the money expended for the purpose of insuring it was in the nature of revenue expenditure incurred solely for earning the profits of the business. It is thus clear that the expenditure was allowed because it was not a capital expenditure. The facts of the other case relied on by the appellant are complicated, and it is not necessary to relate them. But it is clear from the judgment of the Master of Rolls that the deduction claimed in that case was in respect of a payment that was made for, and was directly connected with, the procuring by the assessee company of the advantage of terminating a trading relation and was therefore held to be wholly and exclusively laid out for the purpose of the company's trade. On the other hand, the learned Departmental Representative has cited several cases in support of his contention and we shall notice only those that are more important than the rest. In *Kangra Valley Slate Co., Ltd. v. Commissioner of Income-tax, Punjab*¹, the assessee company incurred a legal expense for defending a suit brought by a village proprietary body to eject the company from certain slate quarries which were their capital asset. The company's claim to deduction of the expense was rejected on the ground that it was a non-recurring outlay required to retain a capital asset. The facts in *Commissioner of Income-tax, Burma v. Gasper and Company, Rangoon*², and *Amrita Bazar Patrika, In re*³, were altogether different and do not furnish any parallel to the present case. In both the cases the expense was incurred for defending criminal charges, and it was held that the sum could not be deducted as an expenditure under Section 10 (2) (ix) of the Income-tax Act. Another case relied on by the learned Departmental Representative was *Magniram Bangor & Co., In re*⁴. The facts in that case were that the assessee who carried on a money-lending business advanced a sum of money to another company which had taken a lease of certain coal bearing land from a zamindar and in order to secure a loan had taken a mortgage of 14 as. share of the salami and royalty of the leasehold and an assignment

(1) (1935) 3 I.T.R. 324.

(2) (1941) 9 I.T.R. 648.

(3) (1940) 8 I.T.R. 100.

(4) (1941) 9 I.T.R. 373.

of the remaining 2 as. share. The assessee company obtained a decree on the mortgage, but, eventually, had to write off their share of the loan as irrecoverable as the mortgagor company had failed. In a suit brought by the zamindar against the assessee company for rents and royalties due to him under the leases the assessee company incurred a legal expense which, however, was disallowed on the ground that it was incurred to prevent a liability arising in the future.

6. These several cases can only be read as illustrating the rule that while expense incurred for trading purposes or for the the purpose of insuring or protecting stock-in-trade of a business is allowable, any expenditure incurred for protecting or defending a capital asset cannot be admitted for deduction under Section 10 (2) (*ix*) of the Income-tax Act. Beyond that they do not help to decide the particular point arising in this case as to whether the expense of the suit against the Binod Mills Limited was or was not in the nature of capital expenditure. The answer to the question would, in our opinion, depend upon the legal character of a trade mark and its value. Apart from making goods permanently identifiable in association with the name, the trade mark familiarises the public with them, so that the name remains fixed in the mind of the customer and the goods remain associated with certain quality or utility. Thus the trade mark has a permanent value as an asset of a business, that is to say, a capital asset. It cannot be regarded as stock-in-trade because a consumer of the goods does not buy the trade mark, the "Nag Ohhap" in this case, but the goods which are branded with the trade mark which in his mind affords a guarantee of their quality. In this respect a trade mark fundamentally differs from a patent. In the case of the former the property and the right to protection are in the device or symbol adopted to designate the goods sold, and not in the article which is manufactured and sold. That article, *i.e.*, dhoties and shirtings in the present case, is open to the whole world to manufacture and sell; and all that the owner of the trade mark is entitled to prevent is the use of his trade mark by other traders such as will lead purchasers to buy, as his, goods which are not his. On the other hand, a patent right protects the substance of the article, *i.e.*, the stock-in-trade and any unauthorised manufacture is prohibited. We point out this distinction because it makes all the difference to the expenditure incurred for the protection of one or the other. In the present case we hold that the trade mark was a capital asset of the appellant company, and, consequently, the legal expense that it incurred for protecting it against infringement by the Binod Mills Limited was a capital expenditure. The Appellate Assistant Commissioner was therefore right in not admitting the deduction,

7. It only remains to dispose of one argument of the learned Advocate for the appellant. He pointed out that a similar expenditure of Rs. 830 was allowed by the Appellate Assistant Commissioner in the assessment of 1936-37. It is not suggested that the Appellate Assistant Commissioner's decision is binding on us, nor that decisions in Income-tax matters are governed by the rule of *res judicata*. The argument of the learned Advocate was that the Department ought not to be allowed to take an inconsistent attitude. In this connection, he cited *In the matter of Charusila Dassi*¹. That was the case of an assessee who had made inconsistent statements regarding the nature of certain income intended to be assessed, and cannot be regarded as an authority on the point urged by the learned Advocate. It must be borne in mind that each year's assessment for the purposes of income-tax is a distinct proceeding, and, therefore, the decision of an Income-tax authority on a particular point in one assessment year can in no sense be regarded as binding upon another authority making the assessment in a subsequent year. The question of finality does not at all arise in such a case. Apart from this, it seems to us that the conclusion reached by the Appellate Assistant Commissioner in the assessment of 1936-37 was inconsistent with the admitted premise with which we started. It was conceded before him that the trade mark was a capital asset of the appellant company and yet the Appellate Assistant Commissioner held that the expense incurred was for the purpose of earning profits or gains and allowable under Section 10 (2) (*ix*). He appears to have been impressed by the argument that the expense was necessary for the purpose of continuing the profits of the company or protecting them from reduction by the Binod Mills Limited having infringed the trade mark. The same argument is addressed to us although in a somewhat different form. But the basic fact still remains that the trade mark is a capital asset of the assessee company; and that being so, any expenditure incurred over it must be regarded as a capital expenditure.

8. Coming to the deduction of Rs. 8,000 claimed by the assessee company in each of the two assessment years, we have stated before that the appellant claimed the deduction of Rs. 45,973 and Rs. 43,626, as expenditure of the Welfare Scheme in the assessments of 1938-39 and 1939-40, respectively. This claim was allowed except the expenditure of Rs. 8,000 in each year. Now it is admitted that this amount includes a sum of Rs. 2,546 debited on account of depreciation of premium of the land on which the Bezon Bagh Settlement stands; Rs. 964 paid for municipal taxes and Rs. 749 for farm expenses, leaving a balance of

(1) (1937) 5 I.T.R. 1.

Rs. 3,741 generally spent on the Welfare Scheme. The first item is an instalment of the premium originally paid by the appellant company to the Government and spread over the period of lease. Besides being a capital outlay, the expense cannot be allowed because it was admittedly incurred as long ago as 1925. The learned Advocate conceded the point and gave up further contest. No argument was addressed to us in regard to the second item of Rs. 964 paid for municipal taxes. As regards the third item of Rs. 749 it was claimed as a part of the expense of the Welfare Scheme being spent upon drainage, etc. But that was not the case made before the Appellate Assistant Commissioner who was told that it was an expense in respect of a vegetable farm maintained by the assessee company for the benefit of its employees. Now there is nothing to show that the company is making a free gift of the vegetables grown upon the land. The contest on this point, too, was practically given up. Then there remains the balance of Rs. 3,741. This was disallowed on the ground that all this money could not be deemed to have been spent solely for the benefit of the company's employees. The amount represents the general expenses incurred on the maintenance of the Bezon Bagh Settlement. It was pointed out that some of the tenements in the Settlement are in the occupation of non-employees. It is, however, common ground that out of the above 220 tenements only 11 are occupied by non-employees. The remaining 4 are respectively allotted to the post-office, the postmaster, a doctor and a nurse attached to the Settlement. Obviously, these persons are accommodated in the Settlement for the benefit of the employees. All that can be said is that the benefit extends to 11 ex-employees of the company. If the total expense were apportioned between the two sets, that deemed to have been incurred for the non-employees would come to a negligible sum. It is, however, difficult to make an apportionment. Accordingly we disallow a sum of Rs. 741 on that account and allow the balance of Rs. 3,000.

9. The result is that we partially accept the appeals and allow the appellant company a deduction of a further sum of Rs. 3,000 in each of the assessments of 1938-39 and 1939-40, and dismiss the rest of the claim in each case.

On the application of the assessee under Section 66 (1) of the Indian Income-tax Act (XI of 1922) the Appellate Tribunal referred the case to the Nagpur High Court.

STATEMENT OF CASE.

We are respectfully making this reference at the instance of the assessee, The Central India Spinning, Weaving and Manufacturing

Company Ltd., under Section 66 (1) of the Indian Income-tax (Amendment) Act, 1922. The assessee's application and the written answer of the Commissioner of Income-tax, C.P. & U.P., are respectively marked Ex. A and B in the appended list.

2. The assessee has formulated five questions stated to be questions of law arising out of our judgment. On the other hand, the Commissioner of Income-tax contends that only one question of law arises, and the rest are either questions of fact, or, do not arise out of our judgment.

3. The reference arises out of an assessment made upon the assessee company for the charge year 1938-39. A copy of the Income-tax Officer's order of assessment is Ex. C, and a copy of that of the Appellate Assistant Commissioner, on appeal, is marked Ex. D. The assessee took an appeal (Regular Assessment Appeal No. 11 C. P. of 1941-42) to the Appellate Tribunal from the Appellate Assistant Commissioner's order, and a copy of our (Bombay Bench) judgment in this connection is marked Ex. E.

4. The contest before us was confined to the assessee's claim to deduct two amounts of Rs. 2,577 and Rs. 8,000 as expenditure incurred for the purpose of earning profits, under Section 10 (2) (*ix*) of the Indian Income-tax Act, 1922, as it stood on 31st March, 1939. The clause has been amended and re-written in the Act of 1939. But in this case we are concerned with the clause as it stood before amendment as the assessment in question relates to the charge year 1938-39.

5. The undisputed facts material to the claim of Rs. 2,577 are stated in paragraph 2 of our judgment. Briefly speaking, the assessee company incurred the expense in the year of account in connection with a suit which they had brought against the Binod Mills Ltd., Ujjain, to restrain them from making use of a trade mark to which the assessee had acquired exclusive right by long user. The Income-tax Officer wrote back the amount without assigning any particular reason for doing so. In appeal, the Appellate Assistant Commissioner also rejected the assessee's claim holding that it was capital expenditure, being a non-recurring outlay for retaining a valuable asset of the company. We accepted this view in appeal before us, and have dealt with this part of the case in paragraphs 4, 5 and 6 of our judgment.* Our finding was that the trade mark was a capital asset of the assessee company; and that, consequently, the legal expense incurred for protecting it against infringement was capital expenditure. In this connection, we mainly relied on *Kangra Valley Slate Co., Ltd. v. Commissioner of Income-tax, Punjab*¹, in which the Lahore High Court held that a non-recurring

* Printed *supra* p. 269 ff.

(1) (1935) 3 I.T.R. 324.

outlay required to retain a capital asset is capital expenditure. In the present application the assessee has cited *Southern v. Borax Consolidated Ltd.*¹, which is an English case recently decided by a single Judge of the King's Bench Division. The learned Judge has held that legal expense incurred by a company for maintenance of a capital asset is properly attributable to revenue inasmuch as such expense does not create any new asset. This view apparently conflicts with that taken in *Kangra Valley case*². The English case had not been reported when the appeal was argued, and, consequently, was not before us. And, at this stage, we are unable to say how far it would have affected our finding even if it had been cited. For, apart from our personal inclinations, we should have been faced with the difficulty of choice between an English decision of a single Judge and that of a Division Bench of an Indian High Court which, as far as we are aware, has not been doubted or dissented from by any other High Court in India, although it was distinguished in *Commissioner of Income-tax, Bihar and Orissa v. Maharajahadhiraja Sir Kameshwar Singh of Darbhanga*³. We would, therefore, respectfully welcome their Lordships' decision on the point.

6. The first question raised by the assessee bears on the claim to a deduction of the legal expense. But the form in which it is expressed lacks precision, since it does not set out the real point that requires to be decided. From paragraph 4 (i) of the application, the assessee's contention appears to be that the legal expense ought to have been admitted to deduction by reason only of the fact that it was incurred for the purpose of earning profits. Generally speaking, almost every expense incurred by a company is with the ultimate object of earning profits. But Section 10 (2) (ix) of the Act of 1922, just as much as Section 10 (2) (xii) of the amended Act, requires another condition to be satisfied, namely, that such expenditure must not be in the nature of capital expenditure, before it can be allowed. There was no contest before us as to the purpose for which the legal expense was incurred in this case. In fact, it was substantially common ground that the assessee company had incurred it for the purpose of preventing loss of profits through an illegal use of its trade mark by another company. Therefore, the real question before us was whether the expense was in the nature of capital expense. We answered it in the affirmative holding that it was incurred for the purpose of protecting a trade mark which, it was not disputed, was a capital asset of the company. Therefore, the question that we propose to submit to their Lordships is—

(1) (1942) 10 I.T.R. Suppl. 1.

(3) (1940) 8 I.T.R. 52.

(2) (1935) 3 I.T.R. 324.

“ Whether on the facts of the case the legal expense of Rs. 2,577 is a revenue expenditure and a proper deduction in computing the taxable income of the assessee company from business ?”

7. The remaining four questions relate to the assessee's claim to an allowance of Rs. 8,000. The assessee company incurs an annual recurring expenditure over a Welfare Scheme which it has made for the benefit of its employees. The material facts are stated in paragraphs 3 and 8 of our judgment. In the year of account the assessee claimed an allowance of Rs. 45,973 as cost of the Scheme. The Income-tax Officer allowed Rs. 37,973 out of the total amount, and wrote back the remaining Rs. 8,000 holding that this part of the expenditure was not proved to have been incurred for the benefit of the employees. The Appellate Assistant Commissioner confirmed the Income-tax Officer's order in this respect. In appeal before us, the assessee company expressly abandoned its claim to a part of the amount, namely, Rs. 2,546. The balance claimed was made up of three items, Rs. 964 paid for municipal taxes, Rs. 744 spent over a farm attached to the employee Settlement and Rs. 3,741 spent on the Scheme generally.

8. The second question raised by the assessee relates to the item of Rs. 964. We disallowed it observing that the point was not argued before us. On this point an unfortunate difference has arisen which we should have been glad to avoid. In the application for reference the assessee company have stated that their Advocate did argue the point, and that he cited *Commissioner of Income-tax, Madras v. Nedungadi Bank Ltd.*¹ in support of his argument. We are, however, quite sure that no argument was addressed, nor any authority cited. Our observation in paragraph 8 of our judgment is supported by the notes of arguments that each of us separately took down in our respective Note Books. In these circumstances, we adhere to the observation that the particular point was not argued before us. We also desire to add that we might have considered the question of allowance on this head, if it was possible to do so at this stage. But that, in our opinion, cannot be done, because a question of law, if any, arising from our consideration of the point at this stage will not amount to a question of law arising out of our appellate judgment such as might be referred under Section 66 of the Income-tax Act. Therefore, the second question formulated by the assessee cannot be said to arise out of our appellate judgment.

9. The third and the fourth questions relate to the item of Rs. 744. It was alleged before the Appellate Assistant Commissioner that the amount had been spent over a farm attached to the Welfare

(1) I.L.R. 47 Mad. 667.

Settlement. We were, however, told that it was the cost of a drainage of the Settlement itself. These facts are not denied in the present application. In view of the inconsistency between the two statements the point was not further argued. We accordingly remarked in paragraph 8 of our judgment that the contest on this point, too, was practically given up. In the present application the assessee company do not deny the two conflicting statements, but, in paragraph 4 (iv), make an attempt to reconcile the two stating that the waste water of the Welfare Colony is led to irrigate a vacant plot of land used as a vegetable farm, instead of being allowed to sink in the Settlement grounds. No such explanation was given to us. We, therefore, think that questions 3 and 4 formulated by the assessee do not arise for reference. Besides, they involve a question of fact as to whether the sum of Rs. 744 was proved to have been spent over a part of the Welfare Scheme. On that question we substantially held in the negative, and no question of law arises.

10. Lastly, as regards the item of Rs. 3,741 it was alleged that this amount had been spent over the Welfare Scheme generally, but no particulars of the expense were furnished before the Income-tax authorities. Admittedly, a few of the tenements in the Welfare Settlement are in the occupation of persons who are not employees of the company, and, therefore, a part of the expenditure could not be said to have been incurred exclusively for the benefit of the employees. Taking into consideration the fact that most of the tenements on the Settlement were occupied by the assessee's employees we made an equitable apportionment by allowing the assessee company an amount of Rs. 3,000 and disallowing a small part, namely, Rs. 741. We fail to see how any question of law arises out of the apportionment that we made, which, in turn, was based upon our finding of fact that all this amount had not been spent for the benefit of the employees. We, therefore, think that questions 2, 3, 4 and 5 formulated by the assessee do not arise for reference.

11. Thus the only question that we respectfully submit to their Lordships is:—

“Whether on the facts of the case the legal expense of Rs. 2,577 is a revenue expenditure and a proper deduction in computing the taxable income of the assessee company from business?”

R. B. D. N. Chaudhari, for the Commissioner.

A. V. Khare, for the assessee.

ORDER.

NIROGI, J.—This case arises on a reference made by the Income-tax Appellate Tribunal (Bombay Bench) under Section 66 (1) of the

"Whether on the facts of the case the legal expense of Rs. 2,577 is a revenue expenditure and a proper deduction in computing the taxable income of the assessee company from business?"

7. The remaining four questions relate to the assessee's claim to an allowance of Rs. 8,000. The assessee company incurs an annual recurring expenditure over a Welfare Scheme which it has made for the benefit of its employees. The material facts are stated in paragraphs 3 and 8 of our judgment. In the year of account the assessee claimed an allowance of Rs. 45,973 as cost of the Scheme. The Income-tax Officer allowed Rs. 37,973 out of the total amount, and wrote back the remaining Rs. 8,000 holding that this part of the expenditure was not proved to have been incurred for the benefit of the employees. The Appellate Assistant Commissioner confirmed the Income-tax Officer's order in this respect. In appeal before us, the assessee company expressly abandoned its claim to a part of the amount, namely, Rs. 2,546. The balance claimed was made up of three items, Rs. 964 paid for municipal taxes, Rs. 744 spent over a farm attached to the employee Settlement and Rs. 8,741 spent on the Scheme generally.

8. The second question raised by the assessee relates to the item of Rs. 964. We disallowed it observing that the point was not argued before us. On this point an unfortunate difference has arisen which we should have been glad to avoid. In the application for reference the assessee company have stated that their Advocate did argue the point, and that he cited *Commissioner of Income-tax, Madras v. Nedungadi Bank Ltd.*¹ in support of his argument. We are, however, quite sure that no argument was addressed, nor any authority cited. Our observation in paragraph 8 of our judgment is supported by the notes of arguments that each of us separately took down in our respective Note Books. In these circumstances, we adhere to the observation that the particular point was not argued before us. We also desire to add that we might have considered the question of allowance on this head, if it was possible to do so at this stage. But that, in our opinion, cannot be done, because a question of law, if any, arising from our consideration of the point at this stage will not amount to a question of law arising out of our appellate judgment such as might be referred under Section 66 of the Income-tax Act. Therefore, the second question formulated by the assessee cannot be said to arise out of our appellate judgment.

9. The third and the fourth questions relate to the item of Rs. 744. It was alleged before the Appellate Assistant Commissioner that the amount had been spent over a farm attached to the Welfare

(1) I.L.R. 47 Mad. 667.

Settlement. We were, however, told that it was the cost of a drainage of the Settlement itself. These facts are not denied in the present application. In view of the inconsistency between the two statements the point was not further argued. We accordingly remarked in paragraph 8 of our judgment that the contest on this point, too, was practically given up. In the present application the assessee company do not deny the two conflicting statements, but, in paragraph 4 (iv), make an attempt to reconcile the two stating that the waste water of the Welfare Colony is led to irrigate a vacant plot of land used as a vegetable farm, instead of being allowed to sink in the Settlement grounds. No such explanation was given to us. We, therefore, think that questions 3 and 4 formulated by the assessee do not arise for reference. Besides, they involve a question of fact as to whether the sum of Rs. 744 was proved to have been spent over a part of the Welfare Scheme. On that question we substantially held in the negative, and no question of law arises.

10. Lastly, as regards the item of Rs. 3,741 it was alleged that this amount had been spent over the Welfare Scheme generally, but no particulars of the expense were furnished before the Income-tax authorities. Admittedly, a few of the tenements in the Welfare Settlement are in the occupation of persons who are not employees of the assessee company, and, therefore, a part of the expenditure could not be said to have been incurred exclusively for the benefit of the employees. Taking into consideration the fact that most of the tenements on the settlement were occupied by the assessee's employees we made an equitable apportionment by allowing the assessee company an amount of Rs. 3,000 and disallowing a small part, namely, Rs. 741. We fail to see how any question of law arises out of the apportionment that we made, which, in turn, was based upon our finding of fact that all this amount had not been spent for the benefit of the employees. We, therefore, think that questions 2, 3, 4 and 5 formulated by the assessee do not arise for reference.

11. Thus the only question that we respectfully submit to their Lordships is:—

“Whether on the facts of the case the legal expense of Rs. 2,577 is a revenue expenditure and a proper deduction in computing the taxable income of the assessee company from business?”

R. B. D. N. Chaudhari, for the Commissioner.

A. V. Khare, for the assessee.

ORDER.

NIXONI, J.—This case arises on a reference made by the Income-tax Appellate Tribunal (Bombay Bench) under Section 66 (1) of the

Indian Income-tax (Amendment) Act, 1922. The question submitted for our opinion is as follows :—

“ Whether on the facts of the case the legal expense of Rs. 2,577 is a revenue expenditure and a proper deduction in computing the taxable income of the assessee company from business ? ”

In the year of account 1938-39 the assessee company incurred an expense of Rs. 2,577 in connection with a suit which they had brought against Binod Mills Ltd., Ujjain, to restrain them from using a trade mark to which the assessee had acquired exclusive right by long user. The assessee company claimed deduction of that amount under Section 10 (2) (ix) of the Act of 1922. Their claim was rejected by the Appellate Assistant Commissioner holding that it was capital expenditure being a non-recurring outlay for retaining a valuable asset of the company. That view was upheld by the Income-tax Appellate Tribunal on the ground that the trade mark was a capital asset of the assessee company and that consequently the legal expense incurred for protecting it against infringement was capital expenditure.

2. The Tribunal rested their decision on *Kangra Valley Slate Co., Ltd. v. Commissioner of Income-tax, Punjab*¹, in which the Lahore High Court held a non-recurring outlay required to retain a capital asset is capital expenditure and it declined to follow *Southern v. Borax & Chemicals, Ltd.*², which is an English case in which a single Judge of King's Bench Division held that legal expense incurred by a company for maintenance of a capital asset is properly attributable to revenue for the reason that such expense does not create any new asset. It is because of the conflict between the two cases and the absence of any authoritative decision by any other High Court in India that the Appellate Tribunal thought it necessary to submit the aforesaid question for the opinion of this Court.

3. The question, how far the expenses incurred in litigation are permissible deductions under the law of Income-tax, is not free from difficulty as the law of Income-tax in British India like that in England makes no express provision in that behalf. The Indian Income-tax Act no doubt gives certain positive directions in Section 10 (2) as regards the deductions that are allowed in computing profits or gains of business, profession or vocation, but the item of legal expenses is not included among those enumerated in that section. It is therefore to be considered whether the deduction for legal expenses could properly be allowed under the omnibus provision embodied in clause (ix) of sub-section (2) of Section 10. It was amended in 1939. Before it was amended it ran as follows :—

(1) (1935) 3 I.T.R. 324 ; I.L.R. 16 Lah. 479. (2) (1942) 10 I.T.R. Suppl. 1.

"Section 10 (2). Such profits or gains shall be computed after making the following allowances, namely:—

(ix) any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains."

As a consequence of the amendment made in 1939 its present form is as under:—

"(xii) any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of such business, profession, or vocation."

The wording of the amended enactment resembles that of the corresponding provision found in Cases I and II, Schedule D, Rule 3, of the English Income Tax Act of 1918 which runs as follows:—

"In computing the amount of the profits or gains to be charged, no sum shall be deducted in respect of—

(a) any disbursements or expenses, not being money wholly and exclusively laid out or expended for the purposes of the trade, profession, employment or vocation."

For the purposes of this case we are concerned with clause (ix) of Section 10 (2) as it stood before the amendment of 1939. Comparing the terminology of this clause with that of the amended clause (xii) of the Indian Income-tax Act and the provision in the English Income Tax Act it would be clear that while the Indian Act makes no express provision for legal expenses the English Act does not make any express prohibition against them.

4. The main problem for consideration is whether in India or in England the legal expenses are such as are attributable to revenue account. On that point as pointed out by Pollock, M.R., in *Atherton v. British Insulated and Helsby Cables, Ltd.*¹, it is not possible to lay down any satisfactory definition. Nevertheless attempts in that direction have been made in England. In *Vallambrosa Rubber Co., Ltd. v. Farmer*², Lord Dunedin laid down a broad test in these words:—

"Now, I don't say that this consideration (namely, that the expenses are all expenses which are necessary every year) is absolutely final or determinative, but in a rough way I think it is not a bad criterion of what is capital expenditure as against what is income expenditure to say that capital expenditure is a thing that is going to be spent once and for all, and income expenditure is a thing that is going to recur every year."

But the efficacy of this test was doubted in *Ounsworth v. Vickers Limited*³, where Mr. Justice Rowlatt observed that the real test was

(1) (1924) 10 Tax Cas. 155 at 179-80.

(3) [1915] 3 K.B. 267 at 273.

(2) (1910) 5 Tax Cas. 529 at 536.

between expenditure which is made to meet a continuous demand for expenditure as opposed to an expenditure which is made once and for all. In *British Insulated and Helsby Cables v. Atherton*¹, Viscount Cave, L. C., pointed out that the criterion suggested by Lord Dunedin was not a decisive one in every case for the obvious reason that in many cases in which the payment though made "once and for all" would be properly chargeable against the receipts for the year and the noble and learned Lord Chancellor sought to lay down the test in these words:—

"But when an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."

In that case the assessee company had established a pension fund for its clerical and technical salaried staff. The fund was constituted by a trust deed which provided that members should contribute a percentage of their salaries to the fund, that the company should contribute an amount equal to half the contributions of the members and that the company should contribute a sum of £ 31,784 to form nucleus of the fund. The company paid that sum (£ 31,784) out of current profits and claimed that it was an admissible deduction in computing its profits. Rowlatt, J., on a case stated by the Commissioners for the Special Purposes of the Income Tax Acts held that the contribution made by the company out of its current profits was revenue and not capital expenditure. The case came up before the Court of Appeal. At the hearing the Attorney-General suggested a definition of capital expenditure as follows:—

"Any money expended upon a business which is intended to and does result in an asset is capital."

Scrutton, L. J., referring to that definition observed that it could not apply to the circulating capital of a trade or business and held that the payment of a large sum of £ 31,784 by the company which they were not under any liability to make was either withdrawal of capital from the business for the purposes of the fund, or capital employed in creating an asset or advantage in the business, something added to the business not in discharge of any existing liability but in the result creating a new asset. Lord Atkinson accepted the view of Scrutton, L. J. That means that the expenditure must be of a kind which is calculated to result in an asset to the company or in some particular advantage

(1) [1926] A.C. 205 at 213.

which would enure permanently or for a long series of years. This test was accepted as sound in *Rhodesia Railways v. Income Tax Collector, Bechuanaland*¹, which was a case of an expenditure of £ 252,174 made in renewing 74 miles of railway track including the supply of new rails, sleepers and fastenings wherever necessary. The renewal brought back the worn track to normal condition and as renewed it was not capable of giving more service than the original line. Lord Macmillan after stating that the expenditure did not result in the creation of any new asset but that it was incurred to maintain the assessee's existing line in a state to earn revenue, observed "Nor do their Lordships agree that expenditure in order to form a permissible deduction must have been incurred in the production of the actual year's income which is the subject of the assessment, if by this it is meant that the benefit of the expenditure must not extend beyond the year of assessment, for very many repairs have the result of enabling income to be earned in future years as well as in the year in which they are effected."

5. The test propounded by Lord Dunedin in *Vallambrosa Rubber Co., Ltd. v. Farmer*², which was found to be inconclusive in England was applied in the *Kangra Valley case*³. In that case the question was whether the expenditure incurred by the assessee company in defending, as lessee of certain land in a village, the suit for possession and injunction instituted by the lessors was deductible under Section 10 (2) (ix) of the Income-tax Act as expenditure incurred solely for earning such profits or gains. The assessee company had secured in perpetuity the land which was the subject-matter of the suit by lease for the purpose of quarrying slate. The land therefore was clearly part of the capital and any attack made on that capital if successful would have resulted in its being a loss to the company. Consequently it could with some propriety be said that it was a capital expenditure in the sense that by expending money in defending the suit once and for all it ensured the land permanently to the company. If the test laid down by Viscount Cave in *British Insulated and Helsby Cables v. Atherton*⁴ were applied perhaps the decision would have been otherwise inasmuch as there was no addition of any asset to the company but only maintenance of its already existing asset.

6. The Lahore case was distinguished in *Income-tax Commissioner v. Kameshwar Singh*⁵. In that case the facts were that a person, who was a share-holder in a company and carried on extensive money-lending business, advanced a loan of rupees ten lacs to the company

(1) [1933] A.C. 368.

(2) (1910) 5 Tax Cas. 529.

(3) (1935) I.L.R. 16 Lah. 479; 3 I.T.R. 324.

(4) [1926] A.C. 205.

(5) (1940) 8 I.T.R. 52; A.I.R. 1941 Pat. 197.

at a time when it was in serious financial difficulties. Some of the share-holders brought a suit against him that the loan of 10 lacs was only a part of the promise made in an alleged agreement under which he was to finance the company and that he had failed to implement his promise. He was therefore sought to be made liable to the extent of Rs. 60 lacs as damages for breach of his agreement. The defendant died pending the suit and was succeeded by the assessee, his son, who was substituted in his place. The suit was eventually dismissed and the assessee claimed to deduct the costs of defending the suit as expenses incurred in the money-lending business. It was held that the money which a banker or a money-lender employed in his business, while it was in one sense capital, was also his stock-in-trade and that the money expended for the purpose of insuring the stock-in-trade of a business must be considered to be expenditure in the nature of revenue expenditure, incurred solely for earning the profits in the business. It was argued on behalf of the Commissioner of Income-tax that, had the suit succeeded, the assessee would have had to part with a large part of his capital and that his primary object in defending the suit was to prevent this loss of capital. Agarwala, J., repelled the contention by saying that the expenditure incurred for securing the assessee against possible loss of his business stock and stores (that is, his stock-in-trade) was allowable and that the expenditure could not be disallowed when it was incurred for the purpose of repelling an actual attack on the assessee's stock-in-trade and held that the deduction claimed fell within Section 10 (2) (ix) of the Income-tax Act. Meredith, J., agreed with the learned Judge on the ground that defence of such suits must be regarded as a necessary though unpleasant part of the business. The case went up to the Privy Council whose decision is reported in *Income-tax Commissioner, Bihar v. Kameshwar Singh*⁴. Lord Thankerton, who pronounced the judgment agreed with the Patna High Court that the money advanced by the money-lender to the company was his stock-in-trade and that the expenditure incurred by him in defending the suit was an expenditure incurred solely for the purpose of profits or gains of the money-lending business.

7. In *Southern v. Borax Consolidated, Ltd.*⁵, the facts were similar to those in the Lahore case. A company acquired land in America for purpose of its business. The company had to defend an action challenging its title to the land and in doing so incurred heavy expenses of £ 6,249. Lawrence, J., who heard the appeal from the General Commissioners, adopted the test laid down in *British Insulated and*

(1) (1942) A.I.R., 1942 P.C. 11; 10 I.T.R., 214.

(2) (1942) 10 I.T.R. Suppl. 1.

*Helsby Cables v. Atherton*¹ and applied in *Rhodesia Railways v. Income Tax Collector, Bechuanaland*², and on a review of the authorities came to the conclusion that the legal expenses which were incurred by the company in defending their title to the land did not create any new asset at all but were expenses incurred in the ordinary course of maintaining the assets of the company. The learned Judge referred to *B.W. Noble, Ltd. v. Mitchell*³, in which Lord Hanworth at page 420 made an observation which is very helpful in the decision of the present case. It is as follows :—

“It is a payment made in the course of business, dealing with a particular difficulty which arose in the course of the year, and was made not in order to secure an actual asset to the Company but to enable them to continue, as they had in the past, to carry on the same type and high quality of business unfettered and unimperilled by the presence of one who, if the public had known about it, might have caused difficulty to their business and whom it was necessary to deal with and settle with at once.”

That was a case in which very large payment had been made to get rid of a director and it was held to be an income payment.

Sargant, L. J., at page 421 said :

“The object, as disclosed by paragraph 9 of the Case, was that of preserving the status and reputation of the Company, which the directors felt would be imperilled either by the other director remaining in the business or by a dismissal of him against his will, involving proceedings by way of action in which the good name of the Company might suffer. To avoid that and to preserve the status and dividend-earning power of the Company seems to me a purpose which is well within the ordinary purposes of the trade, profession or vocation of the Company.”

The judgment in *Southern v. Borax Consolidated Ltd.*⁴, though delivered by a single judge has the support of a long line of authorities which hold that an expenditure to be capital expenditure must be one which is made with a view to bring into existence an asset or advantage for the enduring benefit of a trade and not an expenditure which is incurred in the ordinary course of maintaining the assets of the company or to preserve the status and dividend-earning power of the company.

8. Our attention is invited to, *In re Magniram Bangor & Co.*⁵, where the assessee was joined as defendant as an assignee of the original grantee of the mining leases in a suit for arrears of rent and royalty by the superior landlord. In defending the suit successfully

(1) [1929] A.C. 205.

(2) [1933] A.C. 368 ; 1 I.T.R. 227.

(3) (1927) 11 Tax Cas. 372.

(4) (1942) 10 I.T.R. Suppl. 1.

(5) (1941) I.L.R. 1. Cal. 572 ; 9 I.T.R. 573.

the assessee incurred as costs the sum of Rs. 2,15,176 which he claimed to deduct from his profits. It was held that such expenditure being money spent to prevent further liability for rent and royalty in the future was not deductible expenditure within the meaning of Section 10(2) (ix) of the Income-tax Act, 1922. Their Lordships of the Calcutta High Court declined to follow the cases arising under the English Income Tax Act as a safe guide and held that the legal expenses incurred by the assessee were expenses not incurred solely for the purpose of earning such profits or gains but that they were incurred to prevent losses in the future. The case of *Ward and Company v. Commissioner of Taxes*¹, which was a case decided by the Privy Council on an appeal from New Zealand was followed as the provisions in the New Zealand Land and Income Tax Act, 1916, were in terms similar to clause (ix) of Section 10 (2) of the Indian Income-tax Act, 1922, before its amendment in 1939. In that case a brewery company in New Zealand spent money on publishing anti-prohibition literature just before a poll in which the issue was whether there should be prohibition or not. Lord Cave, who delivered the judgment of the Privy Council, pointed out that the expenditure was not necessary for the production of profit, nor was it in fact incurred for that purpose but that it was a purely voluntary expense incurred with a view to influencing public opinion and consequently that it had not been incurred for the direct purpose of producing profit. Panckridge, J., in the Calcutta case stresses the fact that the incurring of expenses by the assessee was a voluntary act meant to dispose once for all of the claim of the superior landlord for rent and royalty against him. This case can be easily distinguished on the ground that the legal expenses had no direct bearing upon the profits and gains of the business but were intended to secure an enduring benefit of a capital nature which was the test laid down by their Lordships of the Privy Council in *Commissioner of Income-tax, Central and United Provinces v. Messrs. Motiram Nandram*².

9. It is indeed difficult to draw a line of demarcation between what is capital expenditure and what is revenue expenditure. The question assumes ostensibly the form of a question of fact. But since the decision of the question turns upon a principle which the legislature has left it to the judiciary to evolve and apply, it must be treated as involving a point of law. That is how the matter has been regarded in the numerous decisions relevant to the issue. It must be noticed that though the provisions of the Income-tax Act may in their terms appear to be different from those in the English Act the question,

(1) [1923] A.C. 145.

(2) I.L.R. [1940] Nag. 342 at p. 348 ; 8 I.T.R. 132 at p.1138,

whether legal expenses should be treated as capital expenditure or revenue expenditure, is one that arises in both countries and in respect of which the law has made no specific provision. The matter therefore has to be considered on some principle of general application. Whether that principle is evolved by the British or by the Indian Courts is immaterial. If it is found to answer a judicial purpose it cannot be rejected for the simple reason that the letter of the laws in the two countries is different. The highest judicial authority in England, *viz.*, the House of Lords, has on full discussion propounded two tests, one that of Lord Dunedin in *Vallambrosa Rubber Co., Ltd. v. Farmer*¹ and the other that of Lord Cave in *British Insulated and Helsby Cables v. Atherton*². The criterion propounded by Lord Cave has received general support in England and according to it the real test is not whether the money spent once and for all is for the enduring benefit of a trade but whether the money so spent makes an addition to the asset or brings an advantage for the enduring benefit of a trade or, as laid down in *B. W. Noble Ltd. v. Mitchell*³ by Lord Hanworth, it served to remove a particular difficulty and to enable the assessee to continue to carry on the same type and high quality of business or as Sargant, L. J., said, to preserve the status and dividend-earning power of the company.

10. In the present case the assessee had to displace a counterfeit trade mark which prejudicially affected the sale of its goods. The threat was not directed against the capital of the company but against its trade. The capital is concerned with production, while the trade is concerned with selling, with a view to profit, the goods which the assessee has manufactured. The counterfeit trade mark introduced into the market by the assessee's unscrupulous rival must be deemed to have had serious effect on the volume of the sale of the goods manufactured by the assessee. The object of launching legal proceedings against the competitor was to restore the trade to its original standard. It was not merely a voluntary act intended to improve the sales but an act necessary to prevent actual loss in the sales. The drop in the sales impaired directly the dividend-earning power of the company not to speak of its status or reputation, and had nothing to do with its capacity to manufacture them and had no bearing on the capital. The assessee was hit not as an industrialist but as a trader; the expulsion of the counterfeit trade mark from the market by means of litigation in Court did not make any addition to the capital of the company or bring any additional advantage but only removed an impediment in the way of earning legitimate profits by sale of the goods produced by the assessee.

(1) (1910) 5 Tax Cas. 529.

(2) [1926] A.C. 205.

(3) (1927) 11 Tax Cas. 372.

11. In view of the foregoing discussion the answer is that the legal expense of Rs. 2,577 is a revenue expenditure and is a proper deduction in computing the taxable income of the assessee company from the business. The applicant will pay the costs of the non-applicant. Counsel's fee Rs. 50.

DIGBY, J.—I have had the advantage of reading the judgment of my brother Niyogi, J., and concur with his conclusion. I think, though I do not decide, that expenditure incurred in defending a capital asset may in some cases be expenditure of a capital nature, and I consider that a trade mark is a capital asset, but I also feel that an attack on a trade mark made by infringement is to be regarded not as an attack on a capital asset but rather as an attack on existing and future trade and on the value of stock-in-trade, existing and in course of manufacture and to be manufactured in the future. Hence I think that this case falls within the ambit of the Privy Council decision cited (*Income-tax Commissioner, Bihar v. Kameshwar Singh*¹). The word "solely" in Section 10 (2) (ix) of the Act under construction is related to the object of expenditure, the earning of profits and gains, and not to the profits and gains of the particular year in which the expenditure is made and deducted. For, obviously, expenditure of one year, not of a capital nature, may often be intended to have a favourable effect on the next year's profits. A good example would be the ordinary expenses of advertisement. I agree that the expenditure was not in the nature of capital expenditure.

Reference answered accordingly.

[IN THE NAGPUR HIGH COURT.]

BYRAMJI & CO.

v.

COMMISSIONER OF INCOME TAX, C. P. & U. P.

GRILLE, C. J., and PURANIK, J.

January 29, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 33—APPELLATE TRIBUNAL RULES, BB. 17 to 21—APPEAL—APPLICATION FOR LEAVE TO URGE ADDITIONAL GROUND OF APPEAL—FORMAL AMENDMENT OF MEMORANDUM OF APPEAL, STAMP DUTY OR VERIFICATION, WHETHER NECESSARY—DISCRETION NOT EXERCISED JUDICIALLY—INTERFERENCE BY HIGH COURT.

The Appellate Tribunal may grant leave to urge an additional ground of appeal even though it has not been added to the memorandum of appeal by means of a proper amendment. There is also nothing in

(1) (1942) A.I.R. 1942 P.C. 11; 10 I.T.R. 214.

the rules which provides that an application for leave to urge an additional ground should be stamped or verified.

Though it is for the Appellate Tribunal to exercise its discretion in granting leave to urge an additional ground of appeal, this discretion has to be exercised judicially and not arbitrarily, and if it is found that it has been exercised arbitrarily, such exercise of discretion can be interfered with by the High Court.

Where the additional ground of appeal sought to be urged was a question of law which did not involve any further investigation into facts and it was also one going to the root of the matter and the only grounds upon which the Appellate Tribunal refused to grant leave to urge it was that this new ground was not added to the memorandum of appeal by a proper amendment and the application for leave was neither stamped nor verified : Held, that the discretion was not properly exercised and the High Court was entitled to interfere.

Case referred to :—

Commissioner of Income-tax, C. P. & U. P. v. Behari Lal Ramchandra (1937) 5 I.T.R. 417.

Case referred to the Nagpur High Court under Section 66 (1) of the Indian Income-tax Act, 1922. Miscellaneous Civil Case No. 192 of 1942.

JUDGMENT OF THE APPELLATE TRIBUNAL.

The only question that arises in this appeal is whether the rates prescribed by the Finance Act, 1938, should be applied in calculating super-tax upon the appellant's income.

2. The point arises in this way. The appellant's total income for the charge year 1939-40 was computed at Rs. 54,024 from different sources. Rs. 6,900 out of this income represented director's fees received by the appellant in the account year from the C. P. Syndicate, and Rs. 29,298 received as dividends from the same company. Thus the income derived from these two sources aggregated to Rs. 36,198, that is to say, more than half the total income. The Income-tax Officer who made the assessment in the first instance treated the director's fees as salary, which, in our opinion, was not correct. But that point is not material.

3. Section 6, sub-section 4, of the Finance Act, 1939, provided that where more than half the total income of any person consisted of income from salaries, interest on securities or dividends, income-tax for the charge year 1939-40 should be imposed at the rates prescribed by the Finance Act of 1938. In regard to the imposition of super-tax, clause (b) of the sub-section laid down an additional condition to be satisfied by the assessee before super-tax rates prescribed by the Finance Act of 1938 could be applied. That condition was that super-tax had

either been deducted or would have been deductible had the Indian Income-tax Amendment Act, 1939, come into force on the 1st day of April, 1938.

4. The Income-tax Officer who first made the appellant's assessment thought that the appellant had satisfied both these conditions in respect of his income, and charged both the income-tax and super-tax at the rates prescribed in 1938. Later, the Income-tax Officer who made the present assessment thought that the appellant had been under-assessed to super-tax by the application of the old rates inasmuch as, in his opinion, the appellant had not satisfied the condition laid down in Section 6 (4) (b) of the Finance Act, 1939. He accordingly made the present re-assessment under Section 34 of the Act by applying the super-tax rates prescribed by the Finance Act, 1939.

5. Admittedly, the appellant is a resident. Section 18 of the Income-tax Act of 1939 does not provide any machinery for the deduction at source of super-tax on the dividend income of a resident. It follows, therefore, that super-tax would not have been deductible from the dividend income of the account year in question had the Income-tax Act of 1939 come into force on 1st April, 1938. Then as to the director's fees received by the appellant, no super-tax could be deducted from it because the amount did not exceed the minimum not chargeable to super-tax. That also is admitted. But the point made by the appellant is that his dividend income must also be regarded as salary, inasmuch as it is paid by the same company from whom he received the director's fees. Such a proposition is obviously untenable and it was not further pressed.

6. Thus on the only question raised in the appellant's memo, the appeal must fail. The appellant, however, made one more point that the re-assessment in the present case was illegal inasmuch as it amounted to a revision of his first assessment by the application of higher rates which the Income-tax Officer who first made the assessment could as well have adopted. But this point was not taken in the memo of appeal, nor was it added by means of any proper amendment. Doubtless, a point of law can be taken in appeal, but it must be by means of a suitable amendment so that the other side might have a reasonable opportunity to meet it. That was not done. In consequence we could not permit the point being taken.

7. In the circumstances the appeal fails and is dismissed.

At the request of the assessee a reference was made to the High Court.

STATEMENT OF CASE.

"We have the honour to make this reference at the instance of the applicants, Messrs. B. P. Byramji & Co., under Section 66 (1) of the

Indian Income-tax (Amendment) Act, 1922. The application and the written answer filed by the Commissioner of Income-tax, C. P. and U. P. are, respectively, marked Exs. A and B in the appended list.

2. There is substantial agreement between the applicants and the Commissioner as to the question of law that may be referred to their Lordships, although the Commissioner appears to doubt if the question can be said to arise out of our appellate judgment in the applicants' appeal, Regular Assessment Appeal No. 13, C. P., of 1941-42. Broadly stated the point is whether, in the circumstances which will be described presently, the applicants should have been permitted to raise an additional ground in appeal before us.

3. A few undisputed facts will help to introduce the point. An assessment was first made upon the applicants for the charge year 1939-40, on a total income of Rs. 54,024. In virtue of Section 3 of the Income-tax Act the amount of income-tax and super-tax to be charged was according to the rates prescribed by the Finance Act of 1939. But a provision in the latter Act, which it is not necessary to notice for the purpose of this reference, made a concession in respect of incomes derived from certain specified sources and assessed for the year in question by directing that income-tax and super-tax shall be charged at the rates prescribed by the Finance Act of 1938. The Income-tax Officer who made the first assessment thought that the applicants' income was governed by that provision, and determined the tax according to the old rates. Later, however, he appears to have realised his error in this respect, and, in consequence, reopened the assessment under Section 34 of the Act and made a fresh assessment computing the tax at the rates prescribed by the Finance Act of 1939. On appeal, the Appellate Assistant Commissioner confirmed the Income-tax Officers' order. Finally, the applicants took an appeal to the Appellate Tribunal which was also dismissed. A copy of our judgment is appended Ex. C.

4. From the memos of appeal filed before us as well as the Appellate Assistant Commissioner (copies of which are, respectively, Exs. D and E), it will appear that although two grounds were taken before the latter and four before us the only point that they involved was whether the rates of tax to be adopted were those prescribed by the Finance Act of 1938 or the corresponding Act of 1939. In course of his arguments before us the learned Advocate raised a point as to the validity of the applicants' re-assessment under Section 34 contending that it amounted to a revision of the original assessment made by the Income-tax Officer. Doubtless, such a contention went to the root of the matter, and, if accepted, would have resulted in the re-assessment being altogether set aside. But we did not permit the point to

be taken at that stage for reasons which we have stated in para. 6 of our judgment. We reproduce the short paragraph for facility of reference:—

“Thus on the only question raised in the appellant's memo, the appeal must fail. The appellant however, made one more point that the re-assessment in the present case was illegal inasmuch as it amounted to a revision of his first assessment by the application of higher rates which the Income-tax Officer who first made the assessment could as well have adopted. But this point was not taken in the memo of appeal, nor was it added by means of any proper amendment. Doubtless, a point of law can be taken in appeal, but it must be by means of a suitable amendment so that the other side might have a reasonable opportunity to meet it. That was not done. In consequence we could not permit the point being taken.”

5. It was pointed out in the arguments in appeal, as it is in the present application, that the additional ground had been taken before the appeal came up for hearing; and that, therefore, the Departmental Representative had ample opportunity to meet it. From this it might appear as though we had lost sight of that fact when we did not permit the additional ground being taken. At the same time from the observations in our judgment it will be fairly clear that we did not permit the point to be raised because it had not been added by means of a proper amendment. To illustrate this remark, a few facts are necessary to be related. The appeal was fixed for hearing on October 11th, 1941. On 7th preceding, we received by post a letter from the applicants dated October 4, 1941, enclosing the additional ground in question, and asking for leave to add it to the memo of appeal. A copy of the letter together with the ground enclosed is Ex. F. It will be seen that the letter in question is neither stamped nor verified. Neither the applicants nor their representative appeared on October 11. Instead, their representative forwarded a written statement of the applicants together with his own, with a forwarding letter stating that he had nothing to add to what was said in those documents. A copy of the letter is Ex. G. The written statements were substantially arguments in writing. The appeal could not be reached on October 11. It was finally taken up on March 25, 1942. In course of his arguments the learned Advocate took up the ground when we drew his attention to the fact that it had not been added by means of a suitable amendment and that consequently the other side has no reasonable opportunity to meet it. In deciding the point we had in mind the provisions of Section 33 of the Income-tax Act, as amended in 1939, as regards the form of appeal, as well as Rules 17 and 21 made by the Income-tax

Appellate Tribunal in exercise of its powers under Section 5-A (8). We only desire to bring these provisions to their Lordships' notice, without intending to add anything to our judgment.

6. Therefore, the only question of law that we respectfully submit to their Lordships is:—

Question Referred

Whether, in the circumstances of the case, the Bench did not properly use its discretion in not permitting the applicants to take the additional ground not raised in the memo of appeal and not added to it by means of a proper amendment?

JUDGMENT.

This is a reference under Section 66 (1) of the Indian Income-tax Act, 1922, by the Income-tax Tribunal. The question referred for our decision is as under:—

“Whether, in the circumstances of the case, the Bench did not properly use its discretion in not permitting the applicants to take the additional ground not raised in the memo of appeal and not added to it by means of a proper amendment?”

2. The facts of the case which have given rise to this reference may briefly be stated as follows:

An assessment was first made on the applicants for the charge year 1939-40 on a total income of Rs. 54,024. By virtue of Section 3 of the Income-tax Act the amount of income-tax and super-tax to be charged was according to the rates prescribed by the Finance Act of 1939; but a provision in the latter Act made a concession in respect of incomes derived from certain specified sources and assessed for the year in question by directing that income-tax and super-tax shall be charged at the rates prescribed by the Finance Act of 1938. The Income-tax Officer who made the first assessment thought that the applicants' income was governed by that provision and determined the tax according to the old rates. Later, however, he appeared to have realized his error in this respect, and in consequence reopened the assessment under Section 34 of the Act and made a fresh assessment computing the tax at the rates prescribed by the Finance Act of 1939. On appeal the Appellate Assistant Commissioner of Income-tax confirmed the order of the Income-tax Officer. The applicants went up in appeal before the Income-tax Appellate Tribunal, which dismissed the appeal. In the memorandum of appeal filed before the Income-tax Tribunal the only point raised was whether the rates of tax to be adopted were those prescribed by the Finance Act of 1938 or those prescribed by the corresponding Act of 1939. The appeal was fixed for hearing on the 11th

October 1941 before the Tribunal. On the 4th October 1941 the assessee sent by post a letter to the Income-tax Tribunal enclosing an additional ground and begged leave to urge it as an additional ground. This was received by the Income-tax Tribunal office on the 7th October 1941. On the 11th October the case was not heard but the assessee's representative had forwarded a written statement stating that whatever had already been urged by them by way of appeal or by way of additional ground was all that they had to urge. The appeal, however, was taken up for hearing on the 25th March 1942. On this date the assessee's advocate argued all the grounds already mentioned in the memorandum of appeal and also wanted to urge the additional ground of which he had given notice by his letter of the 4th October. The Tribunal stated to the advocate that the additional ground had not been added to the memorandum of appeal by means of a suitable amendment and that consequently the other side had no reasonable opportunity to meet it. On this ground the Tribunal did not allow the assessee's advocate to argue that point.

3. The Tribunal concedes that what the applicants sought to urge by way of an additional ground was a pure question of law and that such a point of law could be taken in appeal. It is also admitted by the Tribunal that the contention raised in the additional ground went into the root of the matter and if accepted would result in the re-assessments being set aside altogether, but that they did not permit that point to be taken because it had not been raised in the memorandum of appeal and had not been added to the memorandum of appeal by means of a proper amendment. In paragraph 5 of its reference the Tribunal has stated that the letter of the 4th October is neither stamped nor verified. The Tribunal in all probability wishes our attention to be directed to this fact, though this is not a fact stated in its order in appeal. Paragraph 6 of its judgment is as follows:—

‘Thus on the only question raised in the appellant's memo, the appeal must fail. The appellant, however, made one more point that the re-assessment in the present case was illegal inasmuch as it amounted to a revision of his first assessment by the application of higher rates which the Income-tax Officer who first made the assessment could as well have adopted. But this point was not taken in the memorandum of appeal, nor was it added by means of any proper amendment. Doubtless a point of law can be taken in appeal, but it must be by means of a suitable amendment so that the other side might have a reasonable opportunity to meet it. That was not done. In consequence we could not permit the point being taken.’

It would thus seem from this paragraph that the question regarding stamp or verification was not present in the mind of the Tribunal

when it disallowed the prayer for urging the additional point of law. Counsel who appeared for the Commissioner of Income-tax has not been able to show us anything either in the Act or the Rules whereunder an application for urging an additional ground of appeal is required to be stamped or verified.

4. An attempt was made to argue that inasmuch as a memorandum of appeal requires to be verified an application whereby an additional ground of appeal is intended to be urged should also be verified. But an application for urging an additional ground is not a memorandum of appeal. The memorandum of appeal was admittedly duly verified, and if the application for urging the additional ground had been allowed the additional ground would have formed part of that memorandum of appeal which had already been verified. At any rate, in the absence of rules or provisions in the Act for verification and court-fee stamp for such an application we are not prepared to hold that it required verification and court-fee.

5. The next question therefore for decision is whether in the circumstances of the case the Bench did not exercise its discretion properly in not permitting the applicants to take the additional ground. In this connexion our attention was invited to the rules framed by the Tribunal, and in particular to Rules 17 to 21. Rule 17 prescribes the form for the memorandum of appeal and the manner in which the memorandum of appeal has to be signed and verified. Rule 18 also deals with the memorandum of appeal. Rule 19 speaks of the copy that has to accompany the memorandum. Rule 20 deals with a fact which is not borne out by or is contrary to the record and directs how that should be stated and supported. Rule 21 is as follows:—

‘The appellant shall not, except by leave of the Tribunal, urge or be heard in support of any ground of objection not set forth in the grounds of appeal; but the Tribunal, in deciding the appeal shall not be confined to the grounds of objection set forth in the grounds of appeal or taken by leave of the Tribunal under this rule.’

This rule is practically in the same words as Order 41, rule 2, of the Civil Procedure Code. It only requires permission of the Tribunal to urge an additional ground. There is nothing in the rule which says that the additional ground has to be added to the memorandum of appeal by means of a proper amendment. Whether to grant leave or not is left to the discretion of the Tribunal. Counsel for the Income-tax Commissioner drew our attention to rule 22 of the rules made by the Tribunal, though the Income-tax Tribunal did not invite our attention to rule 22 but invited our attention only to

Section 33 and rules 17 to 21. Counsel urged that the memorandum of appeal has to be amended as required by rule 22. Rule 22 deals with a memorandum of appeal which has not been drawn up in the prescribed manner and enacts that such a memorandum may be rejected or may, on such terms as the Tribunal may think fit, be returned to the appellant for the purpose of being amended within a time to be fixed by the Tribunal or then and there. This rule has nothing to do with an application for leave to urge an additional ground and is in no way apposite to the circumstances of the case. The Income-tax Tribunal did not therefore refer us to this rule. Section 33 of the Act also refers to the form in which the appeal should be presented and the manner in which it should be verified. That section also has nothing to do with an application for leave to urge an additional ground. All that the assessee appellant is required to do is to place the new ground of appeal before the Appellate Tribunal and ask for leave to urge the same. The Appellate Tribunal was therefore not justified in refusing to grant leave simply because this new ground was not added to the memorandum of appeal by means of a proper amendment.

6. It is conceded by the Tribunal that the question raised in the additional ground is a question of law not involving any further investigation into facts. It is also stated that the contention raised is such as would go to the root of the matter and if accepted would result in the re-assessments being set aside altogether. The contention raised is thus a very important one, and it being a pure question of law the discretion should have been exercised in favour of the assessee, who should have been permitted to urge it. In the Appellate decision it is stated that a point of law, though it can be taken in appeal, can be taken only by means of a suitable amendment so that the other side might have a reasonable opportunity to meet it. It was urged before us that the application was filed on the 4th of October 1941, that it reached the office on the 7th October 1941, that the case was to be heard on the 11th October, and that on that date the Income-tax Department had full notice of the fact that permission to urge such an additional ground was being asked for. There is nothing in the order of the Tribunal to indicate that the Income-tax Officer objected to the grant of leave for urging the new ground. As the Income-tax Department raised no objection to the additional ground and did not suggest that it had no reasonable opportunity of meeting it the Tribunal was not justified in rejecting the very reasonable prayer of the assessee. We are aware of the fact that under the rules it is for the Tribunal to exercise discretion in granting leave to urge an additional ground; but this discretion has to be exercised judicially and

not arbitrarily and if it is found that it has been exercised arbitrarily such exercise of discretion can be interfered with: *Commissioner of Income-tax, U. P. & C. P. v. Behari Lall Ramchandra*¹. The circumstances of this case do not disclose any reason why leave to urge this additional ground should have been refused. The only grounds mentioned in the judgment of the Tribunal have been shown by us to be improper. We have shown that the reason stated in the reference, *viz.*, that the application was neither stamped nor verified, is also not justified by the provisions of, or the rules made under, the Income-tax Act. We have also shown that the Income-tax Department does not appear to have raised any objection to the grant of leave to urge the additional ground; nor do we find any complaint by them that they had no reasonable opportunity of meeting it if it had been urged at that hearing. The assessee had placed on record on the 11th October 1941 a written argument including an argument on this additional ground. The other side had every opportunity of looking at it and knowing what was meant to be urged on that new ground. Under these circumstances our answer to the question referred to for decision is that the Bench did not properly use its discretion in not permitting the applicants to take the additional grounds not raised in the memo of appeal and not added to it by means of a proper amendment. The Income-tax Commissioner shall pay the costs of the assessees, which we fix at Rs. 75 and refund Rs. 100 deposited by the assessees.

Reference answered.

[IN THE PRIVY COUNCIL.]

THE HONOURABLE NAWAB HABIBULLA

v.

COMMISSIONER OF INCOME-TAX, BENGAL.

LORD THANKERTON, SIR GEORGE RANKIN and

Sir MADHAVAN NAIR.

December 14, 1942.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 2 (1), 6—AGRICULTURAL INCOME—WAKF OF AGRICULTURAL PROPERTIES—REMUNERATION PAID TO MUTAWALLI—WHETHER AGRICULTURAL INCOME—SALARY AND AGRICULTURAL INCOME.

One of the ancestors of the assessee had constituted a wakf of agricultural properties, but no remuneration was provided by the

(1) (1937) 5 I.T.R. 417.

wakfnamah for the post of the mutawalli. A suit was filed by some members of the founder's family for removal of the assessee from his office and for accounts. It was compromised and the terms of this compromise which included a scheme for administration of the wakf, provided that the assessee should continue to be the mutawalli and that "the remuneration of the mutawalli payable from the wakf shall be Rs. 2,500 monthly together with a fixed allowance of Rs. 500 per month for conveyance and other personal charges incidental to his position." The question being whether the sum of Rs. 49,500 which the assessee had received under the above mentioned provision was agricultural income within the meaning of Section 2 (1) of the Indian Income-tax Act:

Held, affirming the decision of the Calcutta High Court, that although the income received by the wakf estate was agricultural income within the meaning of Section 2 (1) of the Indian Income-tax Act, the sums drawn therefrom as remuneration by the assessee were not agricultural income. Obiter.—A different question might have arisen if the assessee's remuneration had been by way of a fractional part of the income of the wakf estate, or by a percentage commission.

K. Habibulla, In re (1941) 9 I.T.R. 292 affirmed.

Income-tax Commissioner, Bihar & Orissa v. Maharajadhiraj of Darbhanga (1935) 62 I.A. 215 ; 3 I.T.R. 305 ; 14 Pat. 623, distinguished.

Privy Council Appeal No. II of 1942. Appeal from a judgment of the Calcutta High Court reported as *K. Habibulla, In re*, (1941) 9 I.T.R. 292.

The facts are stated in the judgment.

Sir Thomas Strangman, K.C., and *C. Bagram*, for the appellant.

J. Millard Tucker, K.C., and *Sir Alfred Wort*, for the respondent.

JUDGMENT.

LORD THANKERTON.—The appellant is the hereditary Mutawalli of a wakf estate, and as such he draws remuneration, and the question in the appeal arises on a claim by him that the income thus received by him is exempt from taxation, which came before the High Court of Judicature at Fort William in Bengal on a reference by the respondent, at the appellant's request, under Section 66 (2) of the Indian Income-tax Act, 1922, with a statement of the case and the opinion of the respondent rejecting the appellant's claim to exemption. The question of law referred to the Court was :

"Whether in the facts and circumstances of the case the sum of Rs. 49,500 received by the assessee as his remuneration as Mutawalli was 'agricultural income' within the meaning of Section 2 (1) of the Income-tax Act?"

For the assessment year 1938-39 the appellant was assessed for income-tax purposes on an amount which included the sum of Rs. 49,500 under the head of salaries, which was the appellant's remuneration as Mutawalli for the year of account and included both current salary and arrears. It is admitted that the income of the wakf estate from which the appellant's said remuneration was drawn, was "agricultural income."

The wakf was created by an ancestor of the appellant by a wakf-namah dated the 1st June, 1854. The post of Mutawalli was made hereditary, the wakif's son being first appointed. No benefit was reserved in any way either to the wakif himself or to his descendants and no remuneration was provided for by the wakfnamah for the post of the Mutawalli. In 1925, a suit in the Court of the District Judge, Dacca, in which the removal of the appellant was sought, was compromised on the basis of a Scheme of Administration which had been filed before the High Court and agreed to by all parties, and a decree in terms thereof was made by the District Judge of Dacca on the 24th May, 1928. Under the scheme the appellant's remuneration was provided for as follows :—

"15. The remuneration of the Mutawalli payable from the wakf shall be rupees two thousand five hundred monthly together with a fixed allowance of rupees five hundred monthly for his conveyance the lighting of his apartments, medical attendance and other personal charges incidental to his position....."

It is enough to say that it is clear that under the scheme the appellant has only powers of management of the wakf estate and that those powers are limited in certain respects by the control of a committee of management.

The appellant maintains that the Rs. 49,500 received by him as his remuneration in terms of the Scheme is "agricultural income" as defined in Section 2 (1) of the Act of 1922, and that it is therefore rendered exempt from taxation by Section 4 (3) (viii) of the Act. The relevant part of Section 2 (1) is as follows :

"2. In this Act, unless there is anything repugnant in the subject or context,—

(i) "Agricultural income" means—

(a) any rent or revenue derived from land which is used for agricultural purposes, and is either assessed to land-revenue in British India or subject to a local rate assessed and collected by officers of Government as such."

The High Court rejected the appellant's contention, and their Lordships agree with their conclusion.

The appellant's counsel referred to the recent decision of this Board in *Income-tax Commissioner, Bihar and Orissa v. Mahardjadhiraj of Darbhanga*¹, the judgment being delivered by Lord Macmillan. In that case a money-lender had lent money on a zarpeshgi lease and usufructuary mortgage of agricultural lands under which he was in possession with all the powers of an owner, and upon the terms that, after deducting from a gross estimated rental the estimated costs of management and a sum (thika rent) which was to be credited, he was to take the balance (thika profits). There was no dispute that the rents so drawn by him were agricultural income within the meaning of Section 2 (1) (a) of the Act, and it was conceded that if the assessee had not been a money-lender and the transaction in course of his money-lending business, the statutory exemption would have applied, but it was maintained that the income was income, profits and gains of the business, and that it thereby lost the benefit of the exemption. The Board held that the result of the exemption is to exclude "agricultural income" altogether from the scope of the Act, howsoever or by whomsoever received, and that the nature of the assessee's business cannot affect the exemption.

In the opinion of their Lordships, that case affords a useful contrast to the present case. The position of the assessee in that case had been described by the Chief Justice of Patna—and this Board adopted the description—as follows :

"The mortgagee lessee was to be in possession of both properties, and, in his relation to the cultivators of the soil he stood in the position of landlord dealing directly with them and collecting the rents. He had, moreover, to pay the Government revenue, cesses and taxes and his name was registered in the Land Registration Department. He alone was able to sue for rent whether current or arrears, to sue for enhancement or for ejectment and was able to settle land with raiyats and tenants in all the properties; in fact he was in a position to take all proceedings which the mortgagor would have been able to take in the ordinary course if the lands leased and mortgaged had remained in her khas possession."

Accordingly, the assessee collected the rents directly in his own right, and the amount of his income therefrom depended on his exercise of these rights. The position of the appellant is very different :—the recovery of the rents depends on the rights of the wakf estate, and on the appellant's performance of his duties of management as Mutawalli, and the amount of his remuneration does not depend either on the nature of the properties or assets which constitute the wakf estate, nor

on the amount of the income derived therefrom by the wakf estate. If, as might possibly happen, the whole or a portion of the wakf property ceased to be represented by agricultural lands, it is clear that the remuneration fixed by article 15 of the scheme would not be affected.

Their Lordships agree with the High Court in holding that, albeit the income received by the wakf estate is within the definition of agricultural income in Section 2 (1), the sums drawn therefrom as remuneration by the appellant are not agricultural income received by the appellant, and the question of law referred to the Court should be answered in the negative. Their Lordships desire to add that a different question might have arisen if the appellant's remuneration had been by way of a fractional part of the income of the wakf estate, or by a percentage commission. That case may be considered if, and when, it arises, and their Lordships express no opinion thereon.

Accordingly, their Lordships will humbly advise His Majesty that the judgment of the High Court should be affirmed, and that the appeal should be dismissed with costs.

Appeal dismissed.

[IN THE PATNA HIGH COURT.]

EAST KHAS JHARIA COLLIERY Co., LTD.,

v.

COMMISSIONER OF INCOME TAX, BIHAR AND ORISSA.

HARRIES, C. J., and MANOHAR LALL, J.

April 24, December 21, 1942.

PROFITS—COMPUTATION—CONTRACT TO SUPPLY GOODS—ASSESSEE COMPANY SELLING COAL TO ALLIED COMPANY AT LESS THAN MARKET RATE—SALE OF COAL BY ALLIED COMPANY—HOW PROFIT IS TO BE CALCULATED.

The assessee was a private limited company carrying on a coal mining business and there was another private limited company called the "Khas Company" belonging to the same shareholders and under the same management as the assessee. The assessee returned an income of Rs. 46,922 for the previous year ending 31st March, 1939. On examination of accounts the Income-tax authorities found that the assessee had entered on the credit side a sum of Rs. 67,360 representing the sale price of 33,680 tons of coal at Rs. 2 a ton transferred to the Khas Company. The Income-tax authorities thought that credit should have been given at the prevailing rate of Rs. 4 a ton and they accordingly

added to the assessable income the sum of Rs. 67,360. The assessee contended that they had supplied the coal on the basis of a contract entered into with the Khas Company but they were not able to produce any document except a letter addressed by the assessee to the Khas Company. It was however found on further enquiry that the Khas Company had sold the 33,680 tons of coal to the railway department for the sum of Rs. 109,284 and that charges to the extent of Rs. -/6/- a ton were incurred by that company in effecting the sale of the coal :

Held, that, under the circumstances, the additional sum for which the assessee should have been taxed was Rs. 29,294 (i.e., Rs. 1,09,284—Rs. 67,360) minus the expenses on the sale of 33,680 tons of coal at Rs. -/6/- a ton.

MANOHAR LALL, J.—*If a contract is a genuine contract for the supply of goods for some consideration at a lower rate than that prevailing in the market, it is not permissible to any Court to write out a new contract for the parties.*

Case stated under Section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bihar and Orissa : (Miscellaneous Judicial Case No. 32 of 1941).

STATEMENT OF CASE.

“In compliance with your above letter,* I have the honour to send herewith a statement of the case under Section 66 (3) of the Indian Income-tax Act of 1922 (referred to hereinafter as “the Act”).

2. **Facts of the case.**—The East Khas Jharia Colliery Company, Limited, (hereinafter referred to as the “assessee company”) is a private limited company carrying on coal mining business in Jharia. The question arises in connection with its assessment for the financial year 1939-40. The assessee company filed a return of its income on the 2nd of September 1939, after getting an extension of time from the Income-tax Officer, Dhanbad, on the ground that the audit of its accounts was not complete. The return filed by the company showed a profit of Rs. 46,922-5-1 earned during the “previous” year ended 31st March 1939 (hereinafter referred to as “the accounting year”) and was accompanied by a balance-sheet as at 31st March, 1939 and profit and loss accounts of the two half-years ending on this date. As the Income-tax Officer was not satisfied about the correctness of the return, he issued notices under Sections 23 (2) and 22 (4) of the Indian Income-tax Act, 1922 (hereinafter referred to as “the Act”), for the production of evidence and accounts for the two “previous” years ending 31st March 1939.

* 2251 M.A. dated 30-4-41.

3. While examining the accounts, the Income-tax Officer, Dhanbad, found that, in the accounting year, credit was given to the sales account for a sum of Rs. 67,360, representing the sale price of 33,680 tons of certain kind of coal transferred to the Khas Jharia Colliery (1933) Company, Ltd., (hereinafter referred to as "the allied company"). He was not satisfied as to the *bona fides* of this transaction of sale, said to have been made at an arbitrary rate of Rs. 2 per ton, which was much lower than the rate at which that particular kind of coal was sold to other customers in the same accounting year.

4. The Khas Jharia Colliery (1933) Company, Ltd., is an allied private limited company, belonging to the same shareholders and under the same management as the assessee. It is important to observe that this company has paid no income-tax ever since its first assessment year 1935-36, as its depreciation (both current as well as unabsorbed) exceeded its profits. The Income-tax Officer, therefore, came to the conclusion that the fixation of the sale price of Rs. 2 per ton, in respect of the said 33,680 tons of coal transferred to the allied company, was deliberately made at too low a rate, in order to reduce its own liability to assessment by lowering its own profit and transferring them to the allied company, where they would be wiped out by the heavy depreciation allowance admissible thereto. He estimated the proper sale price at the then reasonable market rate of Rs. 4 per ton. Accordingly he added the difference of Rs. 2 per ton on 33,680 tons, *viz.*, Rs. 67,360, to the income shown by the assessee's accounts. The relevant portion of the assessment order is given in Exhibit A.

5. The assessee company appealed against the said increase in his income, but without any success. It was urged that the allied company obtained a contract from the Bombay Baroda and Central India Railway for the supply of certain quality of coal at Rs. 2-4-0 per ton, and that the said company, therefore, entered into an agreement with the assessee company for the sale of the said coal at Rs. 2 per ton from the latter. The Appellate Assistant Commissioner found the so-called agreement to be no more than '*nudum pactum*' consisting of only a letter, dated 10-11-1937 (copy whereof is Exhibit B) addressed by the assessee to the allied company, and came to the same conclusion to which the Income-tax Officer had come, *viz.*, that the so-called agreement was not a *bona fide* business transaction between the two companies which had allied interest, but it was a device to understate the profits of the assessee company and to thus reduce its own liability to tax, without affecting the assessment of the other company which

was always running at a loss and never assessed to income-tax ever since its incorporation. The relevant portion of the appellate order is given in Exhibit C.

6. Being dissatisfied with the appellate order, the assessee approached me for the necessary relief under Sections 33 and 66 (2) of the Act. On perusal of the records and the proceedings of the case, after hearing the assessee and for the reasons given in my review order, dated 16-9-1940, I declined to interfere with the orders of the lower authorities. Relevant portion of my review order is given in Exhibit D. It may be added that in the preceding year too, the assessee company adopted the same device of understating its own profits to the extent of Rs. 47,680, by transferring 23,840 tons of coal to the allied company at the same ridiculously low price of Rs. 2 per ton. Similar is the case also with the subsequent assessment for the year 1940-41.

7. The assessee company has now filed an application to the Honourable High Court under Section 66 (3) of the Act and I have been directed by the latter to state a case on the following question :—

Question of Law.—“ Whether under the circumstances of the case the Income-tax authorities were entitled to ignore the terms of the agreement entered into between the Khas Jharia Colliery Co. (1933) Ltd., and the assessee company and to add a sum of Rs. 67,860 to the profits of the assessee company for the purpose of assessment to income-tax under the Indian Income-tax Act? ”

8. *Opinion of the Commissioner.*—Since I am required to give my opinion on the above question under the Income-tax law, I may say that in the first instance, no regular agreement or contract said to have been entered into between the assessee company and the allied company was produced before the Income-tax Department, stating that it was a mere verbal agreement. At the time of the interview before me, the assessee-company showed me a copy of the above-mentioned letter, dated 10-11-1937, said to have been written by it to the allied company regarding the sale of certain coal to them. It may be observed that the so-called oral agreement was not proved by means of satisfactory evidence before the Income-tax authorities. Even assuming, though not admitting, that the said letter amounted to the so-called agreement it is to be seen how far there was a genuine contract between the assessee-company and the allied company for the sale of the coal at the uniform rate of Rs. 2 per ton, as mentioned above. It is contended by the assessee-company that the Income-tax authorities are not entitled to go behind the said letter and that they should accept the transaction of sale at the rate of Rs. 2 per ton as

stated in that letter. This proposition has been negatived in more than one High Court. In the matter of *Raja Singh Obera*¹ the Lahore High Court held that the Income-tax Officer had power to call for evidence as to the genuineness of a particular contract and to refuse to recognise the same in the absence of sufficient evidence. A Full Bench of the Calcutta High Court also held in the case of *Bissessar Lal Brij Lal*² that the Income-tax Officer had power to call for evidence over and above a documentary evidence (partnership deed). The Lahore High Court, in the case of *Haji Ghulam Rasul Khuda Baksh*³, held that it was open to an Income-tax Officer in a document (partnership deed) (*sic*) to refuse to recognise such document, if he found that it was not genuine. In *Haji Noor Mohammad Haji Aleemullah*⁴ it was held by the Allahabad High Court that the Income-tax authorities as judges of facts were competent to hold, after going through the evidence placed before them, that the assessee's contention evidenced by the document (partnership deed) was fictitious.

9. It will be seen from the assessment order, appeal order and review order that the assessee-company failed to discharge the onus of establishing that there was a *bona fide* contract to supply the coal to the allied company at the rate of Rs. 2 per ton. The Income-tax Officer enquired into the facts of the case and came to the conclusion that the so-called letter written by the assessee-company to the allied company was not a genuine contract but had been written for the purposes of evading proper taxation. The Income-tax authorities gave weighty reasons in their respective orders for supporting this conclusion and, therefore, refused to recognise the said letter. That the said letter is a sham transaction has been found on the facts of the case by the Income-tax Officer (*vide* Exhibit A), on appeal by the Appellate Assistant Commissioner (*vide* Exhibit C) and in revision by the Commissioner (*vide* Exhibit D).

10. Of course, in such cases, there must be some evidence on which the decision of the Income-tax authorities as judges of fact is reached. In my opinion, such evidence is found in the ample materials and facts given in the assessment order, the appeal order and the review order. I need not add in this connection that the Nagpur High Court held, in the case of *Mulla Fida Ali Sultan Ali*⁵ that if the Income-tax authorities find that a document is sham, or not intended to be acted upon, and there is evidence on which they could arrive at such a finding, the High Court will not weigh the evidence with a view to decide whether the finding is correct or otherwise.

(1) (1934) 7 I.T.C. 357; 2 I.T.R. 331.

(2) (1930) 57 Cal. 1336; 4 I.T.C. 365.

(3) 1937 I.L.R. 19 Lah. 113; 5 I.T.R. 506.

(4) (1937) 10 I.T.C. 426.

(5) (1937) 5 I.T.R. 615.

11. For the reasons given above, it is humbly submitted that the answer to the above question be given in favour of the Crown."

The case came up for hearing before Harries, C. J., and Manohar Lall, J., and the learned Judges passed the following order on 24th April 1942 :—

S. K. Mazumdar, for the assessee.

S. M. Gupta, for the Commissioner.

MANOHAR LALL, J.—The Commissioner of Income-tax was called upon to state a case upon the question "whether under the circumstances of the case the Income-tax authorities were entitled to ignore the terms of the agreement entered into between the Khas Jharia Colliery (1933) Co., Limited, and the assessee company and to add a sum of Rs. 67,360 to the profits of the assessee company for the purpose of assessment to income-tax under the Indian Income-tax Act."

It is only necessary to give the facts shortly in order to show why we are not satisfied that there were sufficient findings in the case as stated to enable us to answer the question satisfactorily and why we propose to ask the Commissioner to re-state the case by giving more specific findings.

The assessee is a private limited company carrying on coal mining business in Jharia. The Khas Jharia Colliery (1933) Company Limited, hereinafter to be referred to as the 'Khas Company,' is an allied private limited company belonging to the same shareholders and under the same management as the assessee.

In connection with the assessment for the financial year 1939-40 the assessee filed a return of his income showing a profit of Rs. 46,922 in the previous year ending 31st March, 1939. An examination of the account showed that the assessee had entered on the credit side a sum of Rs. 67,360 as representing the sale price of 33,680 tons of coal transferred to the Khas Company. The Income-tax Officer thought that credit should have been given not at the rate of Rs. 2 a ton but at the prevailing rate of Rs. 4 a ton. He accordingly added to the assessable income the sum of Rs. 67,360. The assessee's contention was that they sold this quantity of coal to the Khas Company on the basis of a contract into which they had entered with the Khas Company to supply them this coal at Rs. 2 a ton. The assessee failed to convince the Income-tax Officer and the Assistant Commissioner of Income-tax.

The Assistant Commissioner of Income-tax pointed out that no document in support of this agreement had been produced in the course of two years and the agent who appeared before him admitted that the agreement was oral. He, therefore, thought that he could not

reconcile himself to believe that an agreement like this would really take place between two limited companies much less when such a large quantity of coal was involved and for years to come. Accordingly he held that the contract was a mere *nudum pactum* and did not evidence any real transaction.

The Commissioner of Income-tax, however, while refusing to state a case under Section 66 (2) of the Act observed that the agreement was evidenced by a letter addressed by the assessee to the Khas Company. He further observed that the contract rate of Rs. 2 in this agreement was not at all warranted by the average of the actual rates prevailing during the accounting year and that as the Khas Company was incurring heavy losses for some years past it could well afford to enter into this contract with the selling party (the assessee) with the same ownership to buy goods at far below the market rate. It is difficult to understand this criticism. If the contract is a genuine contract for the supply of goods for some consideration at a lower rate than that prevailing in the market, it is not permissible to any court to write out a new contract for the parties.

It will be noticed that neither of the Income-tax authorities who dealt with this question has given any finding as to whether the quantity of coal which was supplied by the assessee to the Khas Company during the previous year was actually sold by the Khas Company to the railway concern at Rs. 2-4-0 a ton or at any higher figure. The assessee in my opinion could not complain if their accounts were recast on the credit side by inserting the price of 33,680 tons of coal at the rate at which the Khas Company sold it to the railway concern and received the price from it in the peculiar circumstances of this case.

For these reasons the Commissioner is directed to restate the case in the light of the observations made above. If there are no materials upon the record to decide this important question it will be open to the Commissioner to make such further enquiries as he thinks fit upon notice to the assessee. If the enquiries are made by the Commissioner direct from the railway concern the Commissioner must hear the assessee after a report has been received from the Railway Company so that the objections of the assessee may be dealt with by the Commissioner at the time of sending up a statement of the case.

The Commissioner is requested to expedite the matter.

HARRIES, C.J.—I agree.

In pursuance of the above order of the High Court the Commissioner submitted the following re-statement of case,

RESTATEMENT OF CASE.

“ With reference to your letter No. 2477 MA dated the 28th April 1942, I have the honour to state that the particulars required by the Hon'ble Judges in their interim order dated 29th April 1942 have been obtained from the Khas Jharria Colliery Co. Ltd. through the assessee company (the East Khas Jharria Colliery Co. Ltd.) and are given as hereunder.

2. During the accounting year ending 31st March 1939, the East Khas Jharria Colliery Co. Ltd. supplied 33,680 tons of coal to the Khas Jharria Colliery Co. Ltd. at Rs. 2/-per ton. Out of this, 16,030 tons were supplied in this first half year ending 30th September 1938 and the remaining 17,650 tons were supplied during the six months thereafter.

During the first half year ending 30th September, 1938, the Khas Jharria Co. sold 18,087 tons in all to the Railway Department as follows :—

| | | | |
|------------------------------------|------------|----|---|
| 7,245 tons at Rs. 2/14 per ton ... | Rs. 20,829 | 6 | 0 |
| 6,019 tons at Rs. 2/8 per ton ... | Rs. 15,047 | 8 | 0 |
| 4,823 tons at Rs. 2/4 per ton ... | Rs. 10,851 | 12 | 0 |

| | | | |
|-------------|------------|----|---|
| 18,087 tons | Rs. 46,728 | 10 | 0 |
|-------------|------------|----|---|

Out of the above stated 18,087 tons, 16,030 tons were supplied by the East Khas Jharria Company, while the balance was purchased from other concerns. The proportionate sale proceeds of 16,030 tons work out at Rs. 41,414.

During the six months ending 31st March 1939, the Khas Jharria Company sold 17,650 tons to the Railway Department as follows :—

| | | | |
|------------------------------------|------------|---|---|
| 213 tons at Rs. 2/14 per ton ... | Rs. 612 | 6 | 0 |
| 391 tons at Rs. 2/8 per ton ... | Rs. 977 | 8 | 0 |
| 3,506 tons at Rs. 2/4 per ton ... | Rs. 7,888 | 8 | 0 |
| 13,540 tons at Rs. 4/5 per ton ... | Rs. 58,391 | 4 | 0 |

| | | | |
|-------------|------------|----|---|
| 17,650 tons | Rs. 67,869 | 10 | 0 |
|-------------|------------|----|---|

It will be seen from the above figures, that the Khas Jharria Company sold 33,680 tons of coal to the Railway Department for Rs. 1,09,284 as shown below :—

| |
|----------------------------|
| 16,030 tons for Rs. 41,414 |
| 17,650 tons for Rs. 67,870 |

| | |
|--------------|---------------|
| 33,680 tons. | Rs. 1,09,284. |
|--------------|---------------|

3. It appears that their Lordships desire to ascertain the proceeds of 33,680 tons of coal sold by the Khas Jharria Colliery Co. to the

Railway Department. It will be seen from the above figures that this quantity of coal was sold by the Khas Jharia Colliery Co., to the Railway Department for Rs. 1,09,284. If this amount was credited to the assessee company's profit and loss account as is suggested in their Lordships' interim order, in lieu of Rs. 67,360, the additional profit to be included in the assessee company's total income will be Rs. 41,924 (Rs. 1,09,284—Rs. 67,360), instead of Rs. 67,360 included by the Income-tax Officer.

4. The papers sent with your letter No. 2633 M.A. dated 6th May 1942 are returned herewith."

The following further facts were subsequently brought to the notice of the learned Judges by the Commissioner.

"I have the honour to refer to my predecessor's letter quoted above in which he reported that the profit made by the East Khas Jharia Colliery Company Limited on the sale of 33,680 tons of its coal to the Railway Department through the Khas Jharia Company Limited amounted to Rs. 41,924 and to state that the assessee company has represented to me that the profit reported is incorrect in that my predecessor through oversight omitted to take into account charges incidental to the sale of coal which were borne by the Khas Jharia Company Limited.

2. I have looked into this contention of the assessee company and find that it is correct. The reported figure of profit therefore requires to be modified. From an inspection of the books of the Khas Jharia Company Limited it appears that charges to the extent of -6/- per ton were incurred by that company in effecting the sale of 33,680 tons of the assessee company's coal to the Railway Department. In view of this fact the amended figure of profit will be as indicated below :—

| | |
|----------------------------------------------------------------|----------------|
| Profit reported by my predecessor | ... Rs. 41,924 |
| Less expenses on the sale of 33,680 tons of coal -6/- a ton | ... Rs. 12,680 |
| Profit actually made | Rs. 29,294 |

I would request you to bring this amended figure of profit to the notice of the Hon'ble Judges at the time the case is taken up by them."

The case then came up for hearing before Harries, C.J., and Manohar Lall, J., and the learned Judges delivered the following judgment on 21st December 1942 :—

S. K. Mazumdar, for the assessee.

S. M. Gupta, for the Commissioner.

JUDGMENT.

MANOHAR LALL, J.—In pursuance of the order passed by this Court on the 24th of April, 1942, the Commissioner of Income-tax has restated the case in which he points out that he is now satisfied, after examining the books of the East Khas Jharria Colliery Company, Limited, that the price of 33,680 tons of coal received by the assessee was Rs. 1,09,284. Therefore, the additional sum for which the assessee should have been taxed is not Rs. 67,360 but Rs. 41,924. This was the statement of the case made by the Commissioner on the 15th of May, 1942. Thereafter another Commissioner succeeded to the office; but he, on examining the records, was satisfied that the contention of the assessee that a deduction from this sum at the rate of six annas a ton for the expenses of the despatch of coal should have been allowed. Accordingly this Commissioner on the 1st of September, 1942, made a report to this Court submitting that the addition of profits should be Rs. 29,294 and not Rs. 41,924.

The assessment on the assessee must, therefore, be reduced by a sum of Rs. 38,576, that is to say, the addition which will be made over and above the figure returned by the assessee under this head will be Rs. 29,294.

As the assessee has succeeded to a large extent in his submissions he is entitled to the costs of the two hearings before this Court. The hearing fee is assessed at two hundred rupees. The assessee is also entitled to the sum of one hundred rupees which he has deposited as fee in order to enable him to make a reference to this Court.

HARRIS, C.J.—I agree.

Assessment reduced.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS

v.

VEDLAPATLA VEERA VENKATARAMIAH AND ANOTHER.

SIR LIONEL LEACH, C. J. and LAKSHMANA RAO, J.

March 15, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922 AS AMENDED IN 1939),
SECS. 22 (4), 23 (2) & (4), 28—NOTICE—NOTICE TO PRODUCE ACCOUNT
BOOKS—NON-COMPLIANCE—IMPOSITION OF PENALTY—CHANGE OF LAW
—APPLICABILITY OF NEW LAW TO ASSESSMENTS FOR PERIODS PRIOR TO
CHANGE—BEST JUDGMENT ASSESSMENT AND IMPOSITION OF PENALTY
FOR NON-PRODUCTION OF ACCOUNTS—QUANTUM OF EVIDENCE RE-
QUIRED,

The assessees filed a return of income for the year 1938-39 and produced certain books of account of their business for the previous year in pursuance of a notice under Sections 22 (4) and 23 (2) of the Income-tax Act served on them on the 11th March 1939. On examination of the books the Income-tax Officer found that the assessees possessed another set of books which they had suppressed and he wrote a letter to them to that effect on 9th December 1939. On 4th January 1940 the Income-tax Officer issued a fresh notice under Sections 22 (4) and 23 (2) of the Act. The assessees did not comply with that notice. The Income-tax Officer thereupon assessed the assessees under Section 23 (4) on 31st January 1940 and subsequently on 21st December 1940 imposed a penalty on them under Section 28 of the Income-tax Act as amended in 1939 for default in compliance with the notice to produce the books of account. On a reference by the Appellate Tribunal:

Held, (1) that as the Income-tax Officer had not made an assessment for the year 1938-39 when the amendment came into force, he was entitled to issue a notice on the 4th January 1940 and he had the right to act under Section 28 (1) (b) as amended for failure to comply with that notice;

(2) that the imposition of a penalty under Section 28 is not a matter of guess work. Before imposing a penalty in such a case as this, the Income-tax Officer must have in his possession such evidence as would convince a reasonably minded man that there exists a second set of books. It is not possible to lay down any hard and fast rule as to what is actually required. Each case must depend upon its own circumstances.

Case referred to :

Commissioner of Income-tax *v.* Badridas Ramrai Shop, Akola (1937) 5 I.T.R. 170; 64 I.A. 102; I.L.R. 1937 Nag. 191; A.I.R. 1937 P.C. 133.

Case referred to the Madras High Court by the Income-tax Appellate Tribunal, Calcutta Bench, under Section 66 (1) of the Indian Income-tax Act, 1922 (XI of 1922), for the decision of the questions of law mentioned in Para. 16 of the Statement of Case: (Case Referred No. 28 of 1942).

JUDGMENT OF THE APPELLATE TRIBUNAL.

Under Section 33 of the Indian Income-tax Act (XI of 1922) the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. Varma (Judicial Member) and P. N. S. Aiyar (Accountant Member), delivered the following Judgment on 20th January 1942.

" This is an appeal against the confirmation by the Appellate Assistant Commissioner of Income-tax, Rajahmundry, of the penalty imposed by the Income-tax Officer on the appellant under Section 28 (1) (b). The Income-tax Officer, Ellore, imposed the penalty on the appellant in respect of the assessment year 1938-39 and directed him to pay a sum of Rs. 1,200/ as penalty under Section 28 (1) (b) of the Amended Act.

2. The appellant contends that the penalty is not leviable as the amended Act is not applicable in respect of the assessment made on the appellant for the year 1938-39. The penalty was imposed in the following circumstances :—

The Income-tax Officer considered that the appellant did not produce all the account books relating to his business in response to the notice he issued under Section 22 (4) and on failure to produce the account books made the assessment under Section 23 (4) of the Income-tax Act. The return was filed before the 1st April 1939 and the notice under Section 22 (4) was issued and complied with as far as the appellant was concerned before 1st April 1939, the date the Amendment Act of 1939 became law.

The contention of the appellant was that there was no book in his possession which he withheld in response to a notice under Section 22 (4). But this was not accepted by the Income-tax Officer for he considered that the default was committed inasmuch as the appellant did not comply with the notice under Section 22 (4). The Income-tax Officer held that the default arose in respect of the notice issued on 4th January 1940 after the amended Act came into force. The appellant further contends before us that the books of account considered to exist did not, in fact, exist and even if the new law be taken to be in force no default was committed by him as the books did not in fact exist.

3. We will first consider whether any default has been committed in non-compliance with the notice under Section 22 (4) of the Act.

(a) The proceedings of this case started on the notice to show cause under Section 28 which requires that the Income-tax Officer should be satisfied that the person has without reasonable cause failed to comply with the notice issued under sub-section (4) of Section 22. There would be no default if the person had no books to produce in compliance with the notice issued to him under sub-section (4) of Section 22 of the Income-tax Act.

4. The Appellate Assistant Commissioner in respect of the assessment of the next succeeding year threw doubt on the existence of the books in the succeeding year although he did not, in so many words, say that he doubted the existence of the books in the year with which

we are concerned in connection with the imposition of the penalty. The question is not free from difficulty for it appears to us that in connection with the imposition of a penalty the existence of the books should be shown in some more tangible material than it may ordinarily be necessary for purposes of an assessment under Section 23 (4). If a person shows accounts and denies the existence of the books in proceedings under Section 28 he cannot prove the negative and some positive material is definitely required to show that the books existed and it is not sufficient to entertain any suspicion, however well founded the suspicion may be. To us it appears that this was not a case for imposition of penalty particularly when the income returned by the appellant was not accepted and assessment was made on a very heavy amount under Section 23 (4) on the supposition that books existed which the appellant failed to produce. It is possible to conceive a case in which Section 23 (4) proceedings may be valid on some material but such materials must lead only to one conclusion of existence of books beyond doubt for imposition of penalty.

5. *The question whether any default was committed after the amended Act came into force?*

The appellant was served with a notice requiring him to produce the books of account under the old Act before the amendment came into force. The notice is dated the 11th March 1939, requiring the appellant to comply with its terms on 20th March 1939. If the books of account existed the default was committed by non-compliance on this date and as at that time no penalty was leviable for non-production of the books he had acquired immunity in respect of this default. When the amended Act came into force the Income-tax Officer issued another notice under Section 22 (4) dated 4th January 1940, requiring production of books on 8th April 1940. This was with a view to bring the case under the amended Act for the default which the appellant committed before. In the case of *Arjun Khemji & Co.*¹, it was ruled by the Judicial Commissioner, Nagpur, that the proceedings initiated under any Act would be governed by the same Act and not by the Amendment Act. The question that was decided in that case was that in respect of proceedings started under the provisions of the Income-tax Act VII of 1918, only the Act VII of 1918 and not the subsequent Act XI of 1922 will apply. On the same lines we hold that the Amended Act of 1939 does not apply in the facts and circumstances of this case.

6. We, therefore, accept this appeal and set aside the order of the Income-tax Officer imposing the penalty. The amount of penalty if paid will be refunded to the appellant."

(1) (1924) 1 I.T.C. 249; 80 I.C. 362.

On the application of the Commissioner of Income-tax under Section 66 (1) of the Indian Income-tax Act (XI of 1922) the Appellate Tribunal referred the case to the Madras High Court.

STATEMENT OF CASE.

“ The Commissioner of Income-tax, Madras, has asked us to state to the High Court of Madras under Section 66 (1) of the Income-tax Act the following questions of law as arising out of our order, dated the 20th January 1942 passed under Section 33 (4) in respect of appeal 28 P. A. No. 1 of 1941-42.

(i) Whether in the circumstances of the case the Income-tax Officer had no jurisdiction to serve the notice under Section 22 (4) dated 4th January 1940 and to direct the payment of penalty for non-compliance with that notice, under Section 28 (1) (b) of the Income-tax Act as amended by Act VII of 1939.

(ii) Whether the Appellate Tribunal is right in holding that in connection with the imposition of penalty under Section 28 (1) (b) for non-compliance of the provisions of Section 22 (4), the existence of the books of account, of which notice to produce has been given, should be shown in some more tangible material than may ordinarily be necessary for the purpose of assessment under Section 23 (4).

or

Whether in the circumstances of the case the Appellate Tribunal was right in holding that there was justification for the respondent not producing the accounts which he had been called upon to produce by the notice under Section 22 (4), dated 4th January 1940.

The respondent has submitted a reply urging that no question of law arises and says the Tribunal has found a question of fact.

2. The question No. 1 as framed does not arise at all. The Tribunal never held that the Income-tax Officer has no jurisdiction to serve notice under Section 22 (4) but what it held was that the repetition of the same notice after the default was actually committed before the Amendment Act of 1939 came into force would not bring the failure within the ambit of the Amendment Act. The second question arises only in case it is held that the Income-tax Act as amended in 1939 applies to the proceedings under reference. We consider that the questions of law do not arise in the form raised but the ones referred to below can be said to arise inferentially from a perusal of the application made. We propose to state the case as under :—

3. The respondent in this case was assessed for the year 1938-39 under Section 23 (4) of the Income-tax Act. The assessment was made under Section 23 (4) as it was alleged that the respondent failed to comply with the terms of the notices issued under Section 22 (4) first

on the 11th March 1939 and second time on the 4th January 1940 requiring him to produce the account books mentioned therein. The respondent had replied that he did not possess the account books mentioned in the notice under Section 22 (4) but this case was not accepted and the assessment was made under Section 23 (4) on 31st January 1940. The respondent preferred an unsuccessful appeal before the Appellate Assistant Commissioner against the assessment under Section 23 (4) and took no further steps. The relevant assessment was for the year 1938-39 commencing from 1st April 1938 and ending on 31st March 1939. It may be pointed out that the notice under Section 22 (4) of the Income-tax Act for production of the account books was first issued on 11th March 1939, requiring the appellant to produce the account books on the 20th March 1939.

4. The Income-tax Officer issued a notice under Section 28 calling upon the appellant to show cause why penalty should not be levied upon him under Section 28 (1) (b) for failure to comply with the notice under Section 22 (4) of the Income-tax Act. One important fact may be mentioned and it is that the Income-tax Officer issued the notice on 4th January 1940 under Section 22 (4) for the second time asking the appellant to produce the same books of account as were called for in the previous notice on 11th March 1939, mentioned above. The respondent pleaded that he had no account books but apparently this case of the respondent was not accepted and a penalty aggregating to the sum of Rs. 1,200 was imposed under Section 28 (1) (b) of the Income-tax Act that came into force on the 1st April 1939.

5. Further from an unsuccessful appeal before the Appellate Assistant Commissioner this matter for the imposition of penalty came up for hearing before this Tribunal and we held that we were not satisfied that this was a case for levy of penalty and as such allowed the appeal of the respondent.

6. The first ground on which the penalty levied was cancelled by this Tribunal was that the proceedings for the levy of penalty in respect of an assessment for the year 1938-39 were governed by the Income-tax Act that was in force in that year and as under the provisions of that Act no penalty could be imposed for the alleged default, the penalty imposed was illegal.

7. The second reason for allowing the appeal of the respondent was, granting for purposes of argument that the Amendment Act of 1939, which came into force on 1st April 1939, and which made the non-compliance of the notice under Section 22 (4) penal, was applicable to this case on the ground that the order under Section 28 was passed in December 1940, the default was committed on the 20th

March 1939, when he had been called upon by the notice of the 11th March 1939, to produce the books and he failed to comply. Assuming that the books of account existed the default was committed on a date prior to the Amendment Act came into force and therefore no offence was committed to apply the Amended Act.

8. Another reason which influenced this Bench of the Tribunal in coming to the conclusion that penalty could not be levied was that existence of the books of account was not established from some tangible materials and that the officers below acted merely on suspicion. The view was that the existence or the non-existence of the books of account in the case of imposition of penalty should *prima facie* be established by the Income-tax Officer for it is not possible for the respondent in this case to take the initial step in penalty proceeding and begin by proving the negative that the books did not exist.

9. Arising out of the above facts three questions of law arise and we would place them in the sequence in which they occur :—

10. *Questions of Law Arising* :—The first question that arises is in regard to the applicability of the particular Act to these penalty proceedings, whether the Act as it stood in 1938-39 or as amended in 1939. The proposition of law may be stated thus :—

Whether the proceedings in this case for the imposition of penalty in respect of the assessment for the year 1938-39 is governed by the Income-tax Act as it stood in 1938-39, the year of assessment or whether they are governed by the Income-tax Act as amended from 1st April 1939, as the proceedings were completed in 1940.

For the reasons stated in our order it was held that the Act as it stood in 1938-39 would apply and the penalty was not imposable.

11. The second is :—

If it is held that the Income-tax Act as amended in 1939 should be applicable the next question will arise :

When was the default committed whether on the 20th March 1939, in answer to the first notice prior to the commencement of the Amended Act of 1939 or in January 1940 when there was again a second default to comply with another notice under Section 22 (4) for the production of the same books.

For the reasons stated in the order we held that the default was committed on 20th March 1939 before the Amendment Act which made the default penal and therefore no penalty would be levied.

12. The third is :—

If it is held that the Amended Act applied whether the view of law taken by the Tribunal that the existence of the books should be shown in some more tangible material than the one in the case of an order

under Section 23 (4) was right in arriving at the conclusion that the case was not a fit one for imposition of penalty.

If it is held that the Amended Act of 1939 is applicable, then the view of law taken by the Tribunal was that the existence of the books of account should be shown in some more tangible manner than it should ordinarily be necessary for the purpose of assessment under Section 23 (4). Section 23 (4) of the Indian Income-tax Act as amended in 1939 reads as follows :—

“If any person fails to make the return required by any notice given under sub-section (2) of Section 22 and has not made a return or a revised return under sub-section (3) of the same section or fails to comply with all the terms of a notice issued under sub-section (4) of the same section or, having made a return, fails to comply with all the terms of a notice issued under sub-section (2) of this section, the Income-tax Officer shall make the assessment to the best of his judgment and determine the sum payable by the assessee on the basis of such assessment and, in the case of a firm, may refuse to register it or may cancel its registration if it is already registered.”

and Section 28 (1) (b) of the same Act reads as :

“If the Income-tax Officer, Appellate Assistant Commissioner or the Appellate Tribunal, in the course of any proceedings under this Act, is satisfied that any person

has without reasonable cause failed to comply with a notice under sub-section (4) of Section 22 or sub-section (2) of Section 23,

he or it may direct that such person shall pay by way of penalty, in addition to any tax payable by him, a sum not exceeding one and a half times the amount of the income-tax and super-tax, if any, which would have been avoided if the income as returned by such person had been accepted as the correct income.”

13. The applicant, the Commissioner of Income-tax, Madras, claims that the language of Sections 23 (4) and 28 (1) are similar and therefore the observation of this Tribunal in their order out of which this reference arises, that the existence of the books of account should be established by a more tangible manner for imposing a penalty under Section 28 than for an assessment under Section 23 (4) is not correct. It should be obvious that the language is not similar and that for mere non-compliance whatever may be the cause an order can be made under Section 23 (4) while an order under Section 28 can only be made if there has been a failure to comply without sufficient cause. The Tribunal therefore made the observation that for an order under Section 28 the existence of the books, the non-production of which will constitute

an offence, must be proved by some more tangible evidence and that a mere suspicion will not be enough to make an order under Section 28. The correctness of this observation, the Commissioner desires to be referred to the High Court for their opinion.

14. In arriving at this finding this Bench of the Tribunal took various facts into consideration. The question about the existence of the account books arose in the following year when the Appellate Assistant Commissioner doubted the existence of the books. The mere fact that the proceedings had been concluded under Section 23 (4) does not make the matter *res judicata* about the existence of the books. The penalty proceedings are altogether different from the assessment proceedings. The question in these proceedings is :—

Whether the assessee failed to comply with the notice without any reasonable cause.

An order under Section 23 (4) can be made if an assessee fails to comply with all the terms of a notice under sub-section (4) of Section 22. The material placed for coming to the conclusion that an order under Section 23 (4) was validly made may or may not be sufficient in certain cases to enable making an order under Section 28. The assessee may not care to proceed further in appeal regarding the particular sub-section (4) of Section 23 under which the order has been made as an appeal in respect of any order passed under Section 23 has been provided for in the Amendment Act of 1939. There is no *res judicata* or estoppel in the income-tax cases or proceedings. In the course of the penalty proceedings the respondent denied the existence of the books of account and the mere suspicion however strong it may be, it is submitted, is not a ground for imposition of penalty and this is what the Tribunal meant in its order dated 20th January 1942. In short the Tribunal was not satisfied from the circumstances and from what the Appellate Assistant Commissioner said in the next following year that the books existed.

15. If the decision of the Tribunal had not been intermixed with this question of law which the Tribunal enunciated in coming to this finding the matter would have been concluded. The Commissioner of Income-tax has asked for the exposition of law from the High Court and we think it fair to state this point also for the decision of the High Court.

16. With this statement of the case we refer the following questions of law to the High Court under Section 66 (2) of the Indian Income-tax Act :—

(i) Whether the proceedings in this case for the imposition of penalty in respect of the assessment for the year 1938-39 are governed

by the Income-tax Act as it stood in 1938-39, the year of assessment or whether they are governed by the Income-tax Act as amended from the 1st April 1939, as the proceedings were completed in 1940.

(ii) If it is held that the Income-tax Act as amended in 1939 should be applicable the next question will arise :

When was the default committed, whether on the 20th March 1939 in answer to the first notice prior to the commencement of the Amended Act of 1939 or in January 1940 when there was again a second default to comply with another notice under Section 22 (4) for the production of the same books.

(iii) If it is held that the Amended Act applied whether the view of law taken by the Tribunal that the existence of the books should be shown in some more tangible material than the one in the case of an order under Section 23 (4) was right in arriving at the conclusion that the case was not a fit one for imposition of penalty.

17. The papers mentioned in the index will form the paper book."

K. V. Sessa Aiyangar, for the Commissioner.

A. Lakshmayya, for the assessee.

JUDGMENT.

(Judgment of the Court was delivered by the Honourable the Chief Justice).

This reference has been made by the Income-tax Appellate Tribunal, Calcutta Bench, under Section 66 (1) of the Income-tax Act at the request of the Commissioner of Income-tax, Madras. On the 15th August 1938 the assessees filed a return of their income for the year 1938-39. On the 11th March 1939 the Income-tax Officer served a notice upon them under Sections 22 (4) and 23 (2) to produce the accounts of their money-lending business for the year 1937-38 and connected documents. The notice was to be complied with by the 20th of that month. The assessees produced for the inspection of the Income-tax Officer certain books of account but when he examined them he considered that the assessees possessed another set of books which they had suppressed. When the notice under Sections 22 (4) and 23 (2) was served on the assessees Section 28 had not been amended. It was amended with effect from the 1st April 1939. Sub-section (1) (b) of Section 28 now provides that if the Income-tax Officer, the Appellate Assistant Commissioner or the Appellate Tribunal in the course of proceedings under the Act is satisfied that a person has without reasonable cause failed to comply with a notice under sub-section (4) of Section 22, or sub-section (2) of Section 23, he or it may direct him to pay by way

of penalty, in addition to the tax payable by him, a sum not exceeding one and a half times the income-tax and super-tax, if any, which would have been avoided if the income as returned by the person had been accepted as the correct income.

On the 9th December 1939 the Income-tax Officer wrote to the assesseees stating that a separate set of account books had been kept and that these had not been produced. On the 4th January 1940 he caused to be issued a fresh notice under Sections 22 (4) and 23 (2) requiring the assesseees to produce the books of account for the years 1937-38, 1936-37 and 1935-36. The assesseees did not comply with this notice. On the 31st January 1940 the Income-tax Officer assessed the assesseees for the year 1938-39 on an income of Rs. 16,100. This assessment was under Section 23 (4). Two days before this assessment was made the Income-tax Officer served a notice upon the assesseees requiring them to show cause why a penalty should not be inflicted under Section 28 (1) (b). The respondents appeared before the Income-tax Officer in compliance with this notice and he gave his decision in an order dated the 21st December 1940. He held that there had been default in compliance with the notice to produce the books of account and consequently he imposed a penalty of Rs. 1,200 in addition to the amount of tax payable under the order of assessment.

The assesseees challenged the correctness of both the orders of the Income-tax Officer in appeals to the Assistant Appellate Commissioner, who agreed with the Income-tax Officer. The assesseees accepted the decision of the Assistant Appellate Commissioner so far as it concerned the assessment to income-tax under Section 23 (4), but they appealed to the Income-tax Appellate Tribunal against the penalty which had been inflicted on them. The Tribunal allowed the appeal on the ground that in connection with the imposition of a penalty for the non-production of books "the existence of the books should be shown in some more tangible material than it may ordinarily be necessary for purposes of an assessment under Section 23 (4)." The Tribunal also held that Section 28 could not be applied in a case where the assessment was for a period prior to the 1st April 1939 when the amendment came into force.

The Tribunal has referred three questions to the Court for decision. They read as follows :—

"(1) Whether the proceedings in this case for the imposition of penalty in respect of the assessment for the year 1938-39 are governed by the Income-tax Act as it stood in 1938-39, the year of assessment, or whether they are governed by the Income-tax Act as amended from the 1st April 1939, as the proceedings were completed in 1940.

(2) If it is held that the Income-tax Act as amended in 1939 should be applicable the next question will arise: when the default was committed, whether on the 20th March 1939 in answer to the first notice prior to the commencement of the amended Act of 1939 or in January 1940 when there was again a second default to comply with another notice under Section 22 (4) for the production of the same books.

(3) If it is held that the Amended Act applied, whether the view of law taken by the Tribunal that the existence of the books should be shown in some more tangible material than the one in the case of an order under Section 23 (4) was right in arriving at the conclusion that the case was not a fit one for imposition of penalty."

It is regrettable that the Tribunal did not take greater care in framing these questions. The second and third questions as they stand are not intelligible; but we gather what is meant from the order which the Tribunal passed on the assessee's appeal.

The first question is whether Section 28 (1) (b) can be applied in respect of the failure to comply with the notice issued on the 4th January 1940. It obviously could not be applied to the earlier notice because when that notice was issued the amendment had not been made. When the second notice was issued the amendment had been made and we consider that the section was applicable. When the amendment came into force the Income-tax Officer had not made an assessment for the year 1938-39 and he was entitled to make it when he did, namely, on the 31st January 1940. It has been suggested that to hold that Section 28 (1) (b) applies to the second notice is making the section retrospective, but this is not so. The Income-tax Officer had full power to issue the notice on the 4th January 1940 and failure to comply with it meant liability under Section 28 (1) (b). The answer to the first question is that the Income-tax Officer had the right to act under Section 28 (1) (b) for failure to comply with the notice issued to the assessee on the 4th January 1940. This answer also covers the second question.

The third question is really whether more evidence is required for the imposition of a penalty under Section 28 than would be required for a "best judgment" assessment under Section 23 (3). The two sections have nothing in common and it is not possible to give a direct answer to the question. When the Income-tax Officer makes an assessment under Section 23 (4) it must be in the nature of an estimate, because the assessee has failed to place before him material for making an accurate assessment. In *Income-tax Commissioner v. Badridas Ramrai Shop, Akola*¹, the Privy Council pointed out how an Income-

(1) (1937) 5 I.T.R. 170 at p. 180; 64 I.A. 104,

tax Officer should proceed when assessing under that section. Their Lordships said :

“ The Officer is to make an assessment to the best of his judgment against a person who is in default as regards supplying information. He must not act dishonestly or vindictively, or capriciously, because he must exercise judgment in the matter. He must make what he honestly believes to be a fair estimate of the proper figure of assessment and for this purpose he must, their Lordships think, be able to take into consideration local knowledge and repute in regard to the assessee's circumstances and his own knowledge of previous returns by and assessments of the assessee, and all other matters which he thinks will assist him in arriving at a fair and proper estimate ; and though there must necessarily be guess-work in the matter, it must be honest guess-work. In that sense, too, the assessment must be to some extent arbitrary.”

The imposition of a penalty under Section 28 is not a matter of guess-work. Before imposing a penalty in such a case as this the Income-tax Officer must have in his possession such evidence as would convince a reasonably minded man that there exists a second set of books. It is not possible to lay down any hard and fast rule as to what is actually required. Each case must depend upon its own circumstances. We answer the third question in this sense.

The Commissioner is entitled to his costs which we fix at Rs. 250.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME-TAX, BOMBAY

v.

MAHOMEDBHOY I. M. ROWJI.

BEAUMONT, C.J., and KANIA, J.

April 8, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 9 (1) (iv)—INCOME FROM PROPERTY—ALLOWANCES—MUNICIPAL TAX PAID UNDER CITY OF BOMBAY MUNICIPAL ACT—WHETHER “AN ANNUAL CHARGE NOT BEING CAPITAL CHARGE”—WHETHER ALLOWABLE DEDUCTION—CITY OF BOMBAY MUNICIPAL ACT (III OF 1888), SEC. 212.

The Municipal tax levied on property under the City of Bombay Municipal Act and which when in arrear becomes a charge on the property under Section 212 of that Act, does not come within the expression “an annual charge not being a capital charge” in Section 9 (1) (iv) of the Income-tax Act, 1922. Consequently, an assessee is not entitled to deduct from his income from property under Section 9 (1) (iv) of the

Income-tax Act, the amount paid by him as municipal general tax in respect of his immoveable property under the City of Bombay Municipal Act.

Case referred to :—

Bejoy Singh Dudhuria *v.* Commissioner of Income-tax, Bengal (1933) I.L.R. 60 Cal. 1029 ; 1 I.T.R. 135 ; 60 I.A. 196 ; 6 I.T.C. 449.

Case referred under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay : (Income-tax Reference No. 4 of 1943).

REFERENCE TO HIGH COURT.

“ MY LORDS,

Under Section 66 (2) of the Indian Income-tax Act, XI of 1922 (hereinafter referred to as “the Act”), and at the instance of Mr. Mahomedbhoy I. M. Rowji (hereinafter referred as “the assessee”) I have the honour to refer for your Lordships’ decision the question of law stated in paragraph 7 below which has arisen from the assessment of the assessee for the financial year 1939-40, the relevant accounting period being the Samvat year 1994.

2. *Facts of the Case.*—Section 140 of the City of Bombay Municipal Act, III of 1888, prescribes three taxes which, shall be levied on buildings and lands in the City and shall be called property taxes,” namely, a water tax, a halalkhore tax and a general tax. Section 197 states that “each of the property taxes shall be payable in advance in half yearly instalments on each first day of April and on each first day of October”; and Section 212 states that “property taxes due under this Act in respect of any building or land shall, subject to the prior payment of the land revenue if any due to the Provincial Government thereupon, be a first charge upon the said building or land and upon the goods and chattels, if any, found within or upon such building or land and belonging to the person liable for such taxes.”

3. During the relevant accounting period the assessee paid to the Bombay Municipality a sum of Rs. 16,870 on account of the municipal general tax on properties belonging to him. He claimed that this sum should be allowed as a deduction against his income from property under the provisions of Section 9 of the Act. The relevant portion of this section, as amended by the Income-tax (Amendment) Act, 1939, reads as follows :—

“9. (1) The tax shall be payable by an assessee under the head “Income from Property” in respect of the *bona fide* annual value of property consisting of any buildings or lands appurtenant thereto of which he is the owner, other than such portions of such property as he may occupy for the purposes of any business, profession or vocation

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(v) any sums paid on account of land revenue in respect of the property."

4. The Income-tax Officer held that the general tax paid to the Bombay Municipality could not be regarded as an annual charge for the purpose of Section (9) 1 (iv) of the Act. He therefore refused to allow the deduction claimed by the assessee and he proceeded to make an assessment on the total income of Rs. 1,56,450, consisting of Rs. 1,26,172 from property and Rs. 30,278 from mortgages and dividends. A copy of the assessment order is annexed and marked A.

6. Being dissatisfied with the decision regarding the property tax the assessee submitted an application to the Commissioner of Income-tax, Bombay, under Sections 33 and 66 (2) of the Act, in which he requested the Commissioner either to exercise his powers of revision or to make a reference to the High Court. A copy of the application is annexed and marked C.

7. *Question for Decision.*—Since I am not prepared to revise the assessment I refer the following question for your Lordships' decision :—

"Whether under the provisions of Section 9 of the Act the assessee is entitled to a deduction of Rs. 16,370, being the municipal general tax paid to the Bombay Municipality in respect of the immoveable property belonging to him."

8. *Opinion of the Commissioner.*—As has already been stated the assessee contends that the municipal general tax is an "annual charge" on his properties within the meaning of Section 9 (1) (iv) of the Act. Since the term "annual charge" has not been defined it has to be interpreted in the light of the other provisions of the Act, and I submit that clause (v) of the same sub-section is of special significance in this connection. Clause (v) allows the deduction of "any sums paid on account of land revenue in respect of the property." Arrears of land revenue have always been considered to be a paramount charge on the land and Section 212 of the City of Bombay Municipal Act, which has been quoted in paragraph 2 above, expressly states that the charge in respect of the property taxes is "subject to the prior payment of the land revenue." Like the municipal general tax land revenue is normally payable twice a year, and if the municipal tax can be regarded as an annual charge it seems clear that the land revenue would also be an annual charge. Hence if the words "annual charge" in clause (iv) could be interpreted as including charges created by the operation of law in respect of arrears of municipal and other taxes clause (v) would be redundant. There would also be an inconsistency in the provisions of the two clauses since clause (v) permits land revenue to be deducted only if it has actually been paid whereas under clause (iv) the amount of the charge would be deductible irrespective of actual payment.

9. I further submit that the Legislature must be presumed to have been aware of the existing state of the law on the subject. In *Krishn Lal Seal In re*¹, the Calcutta High Court had held that in calculating the annual value of property under Section 9 before its amendment an assessee was not entitled to make any deduction on account of the municipal tax payable under Section 149 of the Calcutta Municipal Act of 1923, and this decision had been followed by a Full Bench of the Punjab High Court in *Lalla Mal Sangham Lal v. Commissioner of Income-tax, Punjab*². It therefore seems reasonable to presume that if the Legislature had intended to override these decisions and to allow deductions in respect of municipal taxes it would have made a specific provision for the purpose. This presumption is strengthened by the fact that a specific provision does exist in clause (ix) of sub-section (2) of Section 10, which allows the

(1) (1932) 6 I.T.C. 273.

(2) (1936) 4 I.T.R. 250.

deduction of "any sums paid on account of land revenue, local rates or municipal taxes in respect of such part of the premises as are used for the purposes of the business, profession or vocation." If the intention of the Legislature had been to allow a deduction for municipal taxes as contended by the assessee the natural course would have been to insert a similar provision in sub-section (1) of Section 9 in place of the existing clause (v).

10. Apart from these considerations I submit that the property taxes imposed under the provisions of the City of Bombay Municipal Act become a charge on the property only when they are due and remain unpaid. In other words they are of the nature of a contingent charge. Charges of this nature are distinguishable from charges which exist irrespective of any action that may be taken by the owner and which in effect constitute a burden on the property at all times. In my opinion the provisions of Section 9 (1) (iv) have reference to charges of the latter kind and a charge which is of the nature of a contingent charge is not an "annual charge" within the meaning of that section.

11. For the above reasons, I am respectfully of opinion that the deduction claimed by the assessee is not admissible and that the question which has been stated should be answered in the negative."

Sir Jamshedji Kanga, with N. P. Engineer, Advocate General, for the assessee.

M. C. Setalvad, with G. N. Joshi, for the Commissioner.

JUDGMENT.

BEAUMONT, C. J.—This is a reference made by the Commissioner of Income-tax under Section 66 (2), Indian Income-tax Act, 1922, raising the question :

"Whether under the provisions of Section 9 of the Act the assessee is entitled to a deduction of Rs. 16,370, being the municipal general tax paid to the Bombay Municipality in respect of the immovable property belonging to him?"

Section 9 of the Indian Income-tax Act deals with the heading "Income from property," and directs that the tax shall be payable by an assessee under that head in respect of the *bona fide* annual value of property consisting of any buildings or lands appurtenant thereto of which he is the owner, subject to certain allowances. The only allowance, which, it is suggested, applies to this case, arises under sub-clause (iv), which was amended in the year 1939. The sub-clause reads :

"Where the property is subject to a mortgage or other capital charge, the amount of any interest on such mortgage or charge."

Then the following words were added in 1939 :

"Where the property is subject to an annual charge not being a capital charge, the amount of such charge."

Now, the question is whether any municipal taxes payable under the City of Bombay Municipal Act come within the words "an annual charge not being a capital charge." In order to answer that question one must, in the first place, look at the Municipal Act to see the nature of the taxes imposed.

Sections 126 and 128 of the City of Bombay Municipal Act, 1888, require the Standing Committee to prepare a budget for the ensuing year, and Section 139 defines the taxes which may be levied, which include property taxes, and amongst property taxes is a general tax, and that is the tax which is relevant for the present purpose. Section 143 provides that the general tax shall be levied in respect of all buildings and lands in the city with the exceptions mentioned. Section 146 directs what persons are to be liable for the taxes; in the case of property let, it is the lessor; in the case of property sub-let, the superior lessor; it may in certain cases be the occupier. Then Section 156 requires the Commissioner to keep an assessment book in which the particulars of the various properties and the amounts of assessment have to be entered; and under Section 166 the entries in that book become binding after an opportunity has been given for objections to be lodged and considered. Section 175 and the following sections provide for the case of a building having been vacant for not less than sixty consecutive days, and for the tax having been paid, and provide in such a case for a refund of part of the tax. Section 197 provides that each of the property taxes shall be payable in advance in half-yearly instalments on each first day of April and each first day of October. Then comes Section 212, which is the section creating a charge, and that provides, so far as material, that property taxes due under the Act in respect of any building or land shall, subject to the prior payment of the land revenue due to Government, be a first charge upon the building or land and upon the goods and chattels found within or upon such building or land and belonging to the person liable for such taxes. So that the property tax is leviable in respect of a year, is payable in advance half-yearly on April 1, and October 1, and when in arrear, the tax becomes charge on the property. The question is whether that tax can be said to be "an annual charge not being a capital charge."

I do not find it very easy to say what is the meaning of "an annual charge." The words in their most natural significance would mean a charge arising annually. But charges as a rule do not arise annually. The words, I think, would cover a charge to secure an annual liability, and in that sense it is argued that this tax is an annual charge. It is to

be noticed that the charge only comes into existence when default is made in payment of tax, and naturally ceases as soon as the payment is made. So that the charge is unlikely to endure for a year, since the liability is unlikely to exist for a year. Whether it can be said that this is an annual charge may be doubtful, but it seems to me plain that it cannot be described as "annual charge not being a capital charge." I do not know what meaning can be assigned to the expression in the sub-section "a capital charge," except a charge on capital, though it is not necessary to consider the meaning of the expression except in relation to the charge arising under Section 212 of the Municipal Act. To my mind, such a charge is unquestionably a charge on capital, and, in my view, therefore, one cannot say that the general tax falls within the expression "an annual charge not being a capital charge," which has been added to Section 9 (1) (iv). It is said that those words were added by virtue of the Privy Council decision in *Bejoy Singh Dudhuria v. Commissioner of Income-tax, Calcutta*¹; but if that be so, I think the Legislature must have misunderstood that decision. All that the Privy Council decided in that case was that where a person was entitled to income, and had to pay out of that income an annuity to his father's widow, that annuity was a charge on income, which had in effect priority to his own title, and, therefore, income which was payable to the father's widow never became the income of the assessee liable to assessment under the Act. That case was not dealing with allowances.

The question whether municipal taxes ought to be made the subject of an allowance can hardly have been absent from the minds of the Legislature when they amended Section 9 (1) (iv), Income-tax Act, because Section 9 (1) (v) allows a deduction in respect of any sums paid on account of land revenue, and land revenue for this purpose is on much the same footing as municipal taxes. Moreover Section 10, which deals with allowances which may be claimed by a person assessed in respect of a business, allows deduction of any sums paid on account of land revenue, local rates or municipal taxes in respect of such part of the premises as is used for the purposes of the business. So that it cannot, I think, be questioned that the Legislature had in mind the question whether an allowance should be made in respect of local rates or municipal taxes, and it is, to my mind, inconceivable, if they had meant to allow a deduction of that nature, that they would not have said so in express words. The general nature of deductions allowed from what is assessable income seems to me to be (a) payments necessary to preserve the property, such as payments for ground rent and interest on mortgages and (b) payments necessary in order to enable the income to be

(1) (1933) I.L.R. 60 Cal. 1029; 1 I.T.R. 135.

earned or received. That seems to be the general principle underlying the deductions allowed by the Act, and, it is difficult, to my mind, to say that payment of municipal taxes falls within such a principle; so that I should not expect to find such taxes allowed as a deduction. The payment of municipal taxes results in the provision of various amenities for the property in respect of which they are paid, and if those amenities were not provided by the Municipality, they would have to be provided in many cases by the owner, and there is no heading under which such payments could be claimed as deductions in respect of income-tax. Therefore, if the Legislature were minded to authorise a deduction in respect of municipal taxes, I should have expected them to say so in clear language, and there would be no difficulty in drafting a sub-section covering the point. I find it impossible to suppose that the Legislature, whatever they may have intended the words to cover, can have intended to include municipal taxes in such an expression as "an annual charge not being a capital charge." It is not necessary for us to consider what the exact meaning of those words is. It is sufficient to say that they do not cover municipal taxes which are made a charge on property under Section 212 of the Bombay Municipal Act.

That being so, the answer to the question raised must be in the negative.

The assessee to pay costs.

KANIA, J.—I agree that the answer should be as stated in the judgment of the learned Chief Justice. I do not propose to accept the burden of defining what would fall within the amending words in clause (iv) of Section 9. To say the least it is drafted very inartistically. The expressions "annual charge" and "not being of a capital nature" are not defined anywhere. One can understand annual payment or annual receipt. I do not see how a charge can be annual unless it means a charge in respect of a payment to be made annually. The different meanings given to the word "annual" in Murray's English Dictionary do not fit in with "charge" unless the meaning indicated above is given to the expression "annual charge." In considering the nature of this charge, it has to be noted that in the first instance the tax is fixed for a whole year, but it is liable to be varied under the power of increasing taxation, when necessary. It is also liable to be reduced if the property remains vacant for the different periods mentioned in the Municipal Act. Again, there is no charge at all till the tax has become due. That is made clear by the words of Section 212 of the City of Bombay Municipal Act. If, therefore, a landlord had paid a sum in advance, and on the Municipality fixing the sum of the tax before April 1 in a year, the landlord wrote to the Municipality to

appropriate what he had paid in advance against the tax for the whole year, there will be no charge at all. The fact that the tax can be paid in two instalments makes the position peculiar. After the tax is fixed for the year suppose a payment is made for the first half-year, but not for the second half; under Section 212 of the Municipal Act it is clear that there is a charge on the property for what remains due for the second half. Still, it will not be for the annual payment and therefore not an annual charge. One of the recognised meanings of the word "annual" is "anything that lasts for a year." In my opinion, therefore, the nature of the tax imposed by the Municipal Act does not bring it under the category of annual charge.

The words "not being of a capital nature" also are not clear. For myself, I do not accept the contention that a document which provides that a certain payment to be made monthly or annually and charged on the immoveable property or the estate of an individual, *e.g.*, a charge declared under an agreement or a decree in favour of a Hindu widow for her maintenance, is a document creating a charge of capital nature. I limit this decision expressly to the words used in Section 212 of the City of Bombay Municipal Act, and having regard to the nature of the tax contemplated by the sections of that Act. The point under consideration, in my opinion, is not free from doubt, but having regard to the fact that in Section 10 there is express provision for the allowance of land revenue, local rates or municipal taxes on the property used for business, profession or vocation, if the Legislature were so minded they could have used the same words in clause (iv) of Section 9, if a similar allowance was intended there. I think it is highly desirable for the Legislature to make clear what is intended to be covered by the clause inserted in amending Section 9 (iv).

Reference answered accordingly.

[IN THE PRIVY COUNCIL.]

INDIAN IRON & STEEL CO., LTD.

v.

COMMISSIONER OF INCOME-TAX, BENGAL.

LORD ATKIN, LORD RUSSELL OF KILLOWEN and LORD PORTER.

March 25, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 10 (2) (vi), 26—
DEPRECIATION ALLOWANCE—SUCCESSION TO BUSINESS DURING AC-
COUNTING YEAR—WHETHER SUCCESSOR ENTITLED TO BENEFIT OF
UNABSORBED DEPRECIATION OF PREDECESSOR—COMPUTATION OF
DEPRECIATION—"ORIGINAL COST TO ASSESSEE"—WHETHER ORIGINAL

COST TO PREDECESSOR OR SUCCESSOR—PROPER METHOD OF COMPUTATION—MEANING OF "ASSEESSEE."

By an agreement dated 8th September 1936, made between the appellant company and another company named the Bengal Iron Company Ltd., the former agreed to acquire and take over the whole of the property and assets of the latter as existing on the date of transfer. In pursuance of this agreement the Bengal Company transferred all its property and assets on the 2nd December 1936, to the appellant company which continued to carry on the business of the Bengal Company as part of and in combination with its existing business. The agreement contained a clause assigning 'so far as capable of being assigned, any claim which the Bengal Company may have in respect of unabsorbed depreciation allowances.' At the time of the amalgamation the Bengal Company had to its credit unabsorbed depreciation allowance to the extent of Rs. 85,45,150 which it could set off against its future profits. Similarly, the appellant company had an unabsorbed depreciation allowance of Rs. 62,00,775. Held, by the Judicial Committee, affirming the decision of the High Court of Calcutta, (i) that the appellant company was not entitled to have the depreciation allowance of the Bengal Company computed on the original cost of such assets to the Bengal company for the whole of the previous year but only up to the date of succession and that after that date it had to be computed on the original cost to the appellant company; (ii) that the appellant company was not in law entitled to carry forward the unabsorbed depreciation allowance of the Bengal Company.

Though the word 'assessee' in Section 10 (2) must, when there is a successor to the business charged to tax, be read in certain of the paragraphs as including both predecessor and successor, it does not follow as a consequence that the unabsorbed depreciation of the predecessor must be added to that of the successor or that even in a case when the only business concerned is that which is transferred, the business when transferred carries to the purchaser its unabsorbed depreciation.

Section 26 is concerned not with the computation of tax, but with the person upon whom the liability is imposed. It is only when the person to pay has been ascertained that the terms of Section 10 become material in order to discover how the amount to be paid is to be computed.

The true meaning of Section 26 and Section 10 (2) is that the profits of the predecessor are to be ascertained in accordance with the provisions of Section 10 for the period during which it carried on the business and the profits of the successor are to be ascertained for the period during which it carried on that business in accordance with the same principles. By adding the liability for the former period to the liability for the latter period, the successor will be assessed as if it had

been carrying on the business throughout the year within the meaning of Section 26.

For the purposes of computing depreciation in cases of succession, 'cost to the assessee' means cost to the predecessor so long as he continued to be the owner of the property. But once the property has passed to the successor, he is the assessee and depreciation is to be calculated on the cost to him and not on the cost to his predecessor.

Commissioner of Income-tax v. Buckingham and Cagnatic Co. Ltd. [1935] (63 I. A. 74; 3 I. T. R. 384) and Commissioner of Income-tax v. Masagaon Dock Ltd., [1938] (I. L. R. 1938 Bom. 374; 6 I. T. R. 124) approved; In re Kamlapat Motilal [1939] (7 I. T. R. 374) disapproved. Indian Iron and Steel Co., In re [1941] (9 I. T. R. 539) affirmed.

Appeal (P. C. Appeal No. 7 of 1942) against the Judgment of the Calcutta High Court in Reference No. 13 of 1940 reported as *Indian Iron and Steel Co., In re [1941] (9 I. T. R. 539)*.

Roland Burrows, K. C., Reginald Hills and W. W. K. Page, for the appellant.

J. Millard Tucker, K. C., U. Sen Gupta and N. E. Mustoe, for the respondent.

JUDGMENT.

LORD PORTER.—The Appellant is a Company incorporated and registered under the Indian Companies Act in the year 1918. It carried on the business of an iron-founder and steel maker at Hirapur in the Province of Bengal.

By an agreement dated the 8th September, 1936, made between the appellant and a company named the Bengal Iron Company, Ltd., the former agreed to acquire and take over the whole of the property and assets of the latter as existing on the date of transfer.

This second company was incorporated and registered in England and had carried on at Kulti in the same Province a business similar to that of the appellant. On the 2nd December, 1936, in pursuance of this agreement, and after it had been sanctioned by the High Court in England, the Bengal Company transferred to the appellant the whole of its undertaking and assets, and from the 3rd December (1) the appellant carried on the business previously carried on by that company as part of and in combination with its own existing business, and (2) the Bengal Company ceased to carry on business and went into voluntary liquidation.

In addition to the provisions already set out, the agreement of the 8th September contained (*inter alia*) a further clause assigning, "so far as capable of being assigned, any claim which the Bengal Company may have in respect of unabsorbed depreciation allowances." These allowances are those specified in Section 10 of the Indian Income-tax

Act, 1922, a section which, so far as is material, contains the following provisions :

10. (1) The tax shall be payable by an assessee under the head "Business" in respect of the profits or gains of any business carried on by him.

(2) Such profits or gains shall be computed after making the following allowances, namely :—

(i) any rent paid for the premises in which such business is carried on, provided that, when any substantial part of the premises is used as a dwelling house by the assessee, the allowance under this clause shall be such sum as the Income-tax Officer may determine having regard to the proportional part so used.

(ii) in respect of repairs, where the assessee is the tenant only of the premises, and has undertaken to bear the cost of such repairs, the amount paid on account thereof, provided that, if any substantial part of the premises is used by the assessee as a dwelling-house, a proportional part only of such amount shall be allowed.

(vi) in respect of depreciation of such buildings, machinery, plant, or furniture being the property of the assessee, a sum equivalent of such percentage on the original cost thereof to the assessee as may in any case or class of cases be prescribed :

Provided that—

(a) the prescribed particulars have been duly furnished ; (b) where full effect cannot be given to any such allowance in any year, owing to there being no profits or gains chargeable for that year, or owing to the profits or gains chargeable being less than the allowance, the allowance or part of the allowance to which effect has not been given, as the case may be, shall be added to the amount of the allowance for depreciation for the following year and deemed to be part of that allowance, or, if there is no such allowance for that year, be deemed to be the allowance for that year, and so on for succeeding years ; and (c) the aggregate of all such allowances made under this Act or any Act repealed hereby, or under the Indian Income-tax Act, 1886, shall, in no case, exceed the original cost to the assessee of the buildings, machinery, plant, or furniture, as the case may be ;

(vii) in respect of any machinery or plant which, in consequence of its having become obsolete, has been sold or discarded, the difference between the original cost to the assessee of the machinery or plant as reduced by the aggregate of the allowances made in respect of depreciation under Clause (vi) or any Act repealed hereby, or the Indian Income-tax Act, 1886, and the amount for which the machinery or plant is actually sold, or its scrap value ;

(vii-a) in respect of animals which have been used for the purpose of the business otherwise than as stock in trade and have died or become permanently useless for such purpose, the difference between the original cost to the assessee of the animals, and the amount, if any realised in respect of the carcasses or animals.

In a case where a company continues to carry on its own business the principle for computation of these allowances is reasonably well settled, but where one company absorbs another at the end or in the course of a current fiscal year difficulties have from time to time arisen as to the correct allowances to be made.

The statutory provision dealing with the liability to tax of a company whose business is transferred at these times is contained in Section 26 (2) of the same Act and is as follows:—

“26. (2) Where, at the time of making an assessment under Section 23, it is found that the person carrying on any business, profession or vocation has been succeeded in such capacity by another person, the assessment shall be made on such person succeeding, as if he had been carrying on the business, profession or vocation throughout the previous year, and as if he had received the whole of the profits for that year.”

The question for their Lordships' determination is to ascertain the true construction to be placed upon the two sections quoted when read together and to determine the principle upon which depreciation is to be computed and allowed in the case of such a change.

After the amalgamation of the two companies an assessment was made upon the appellant company for the year 1937-38, based upon the figures of the previous year, April 1st 1936, to March 31st, 1937, the year in which the transfer took place. Against this assessment the Indian company appealed and the Assistant Commissioner of Income-tax made an altered assessment which has been summarised in a case afterwards stated by the Commissioner on the 19th December, 1940.

Before the summarised conclusions arrived at by the Assistant Commissioner are set out it is desirable to state the relevant facts and the contentions put forward on behalf of each of the parties.

Up to the time of the amalgamation neither company had been very successful, with the result that each had acquired under Section 10 (2) (vi) a large unabsorbed depreciation allowance. By the end of the fiscal year 1935-36 this allowance in the case of the Bengal Company had reached the figure of Rs. 85,45,150, and in the case of the Indian Company amounted to Rs. 62,00,775. Admittedly as at that date each of those two separate companies could have claimed to set off against any future profit made by it the depreciation allowance to which it

was then entitled. The question now in dispute arises as to the amount of benefit to which the combined companies, if they may be so described, are entitled at the end of the next fiscal year and how much of that amount can be carried on to future years. The appellant maintained that it must be assessed under Section 26 (2) in respect of the business of the Bengal Company as if it had been carrying on that business as a separate activity for the whole year and had received the whole of the profits for that year.

The profits, it is alleged, of the Bengal Company's business had to be ascertained up to the end of the 2nd December, 1936; to those profits must be added the proper proportion of the profits of the combined businesses attributable to the Bengal Company's portion of it, calculated in accordance with the method adopted in *Bell v. National Provincial Bank*¹. From the total yearly profits of that business, ascertained in that way, the appellant was entitled to have the advantage of deducting the previously ascertained unabsorbed depreciation allowance of Rs. 85,69,148, and also further depreciation allowances for the current year, calculated over the whole of the period upon the original cost to the Bengal Company of the assets upon which depreciation was allowable.

Similarly, it was said, with reference to the Indian Company the profits must be ascertained by the same method of computation, and were subject to the deduction of the original unabsorbed depreciation allowance allotted to that company of Rs. 62,00,775, together with the appropriate depreciation for the current year calculated upon the same principles as those adopted in the case of the other company. The profits and allowances having been ascertained in this way, the appellants contended that the lesser sum, *i.e.*, profits, should be deducted from the greater, *i.e.*, the unabsorbed depreciation allowance, and the resultant figure carried forward to the next year, the appellant being thus entitled to the future benefit of both sets of unabsorbed depreciation allowance as a deduction from its future profits.

The respondent, on the other hand, asserted that the correct method to adopt was to find the profits of the Bengal Company for the 8 months from the 1st April to the 2nd December, 1936, and to deduct the resultant figure from the unabsorbed depreciation allowance standing to the credit of that company on the 1st April, 1936, together with the further proper depreciation to be allowed to that company for the same 8 months, calculated on the original cost of those assets to that company. This calculation admittedly would result in a minus figure, but, said the income-tax officials, no further benefit of this unabsorbed depreciation was to be given to anyone.

(vii-a) in respect of animals which have been used for the purpose of the business otherwise than as stock in trade and have died or become permanently useless for such purpose, the difference between the original cost to the assessee of the animals, and the amount, if any realised in respect of the carcasses or animals.

In a case where a company continues to carry on its own business the principle for computation of these allowances is reasonably well settled, but where one company absorbs another at the end or in the course of a current fiscal year difficulties have from time to time arisen as to the correct allowances to be made.

The statutory provision dealing with the liability to tax of a company whose business is transferred at these times is contained in Section 26 (2) of the same Act and is as follows:—

“26. (2) Where, at the time of making an assessment under Section 23, it is found that the person carrying on any business, profession or vocation has been succeeded in such capacity by another person, the assessment shall be made on such person succeeding, as if he had been carrying on the business, profession or vocation throughout the previous year, and as if he had received the whole of the profits for that year.”

The question for their Lordships' determination is to ascertain the true construction to be placed upon the two sections quoted when read together and to determine the principle upon which depreciation is to be computed and allowed in the case of such a change.

After the amalgamation of the two companies an assessment was made upon the appellant company for the year 1937-38, based upon the figures of the previous year, April 1st 1936, to March 31st, 1937, the year in which the transfer took place. Against this assessment the Indian company appealed and the Assistant Commissioner of Income-tax made an altered assessment which has been summarised in a case afterwards stated by the Commissioner on the 19th December, 1940.

Before the summarised conclusions arrived at by the Assistant Commissioner are set out it is desirable to state the relevant facts and the contentions put forward on behalf of each of the parties.

Up to the time of the amalgamation neither company had been very successful, with the result that each had acquired under Section 10 (2) (vi) a large unabsorbed depreciation allowance. By the end of the fiscal year 1935-36 this allowance in the case of the Bengal Company had reached the figure of Rs. 85,45,150, and in the case of the Indian Company amounted to Rs. 62,00,775. Admittedly as at that date each of those two separate companies could have claimed to set off against any future profit made by it the depreciation allowance to which it

was then entitled. The question now in dispute arises as to the amount of benefit to which the combined companies, if they may be so described, are entitled at the end of the next fiscal year and how much of that amount can be carried on to future years. The appellant maintained that it must be assessed under Section 26 (2) in respect of the business of the Bengal Company as if it had been carrying on that business as a separate activity for the whole year and had received the whole of the profits for that year.

The profits, it is alleged, of the Bengal Company's business had to be ascertained up to the end of the 2nd December, 1936; to those profits must be added the proper proportion of the profits of the combined businesses attributable to the Bengal Company's portion of it, calculated in accordance with the method adopted in *Bell v. National Provincial Bank*¹. From the total yearly profits of that business, ascertained in that way, the appellant was entitled to have the advantage of deducting the previously ascertained unabsorbed depreciation allowance of Rs. 85,69,148, and also further depreciation allowances for the current year, calculated over the whole of the period upon the original cost to the Bengal Company of the assets upon which depreciation was allowable.

Similarly, it was said, with reference to the Indian Company the profits must be ascertained by the same method of computation, and were subject to the deduction of the original unabsorbed depreciation allowance allotted to that company of Rs. 62,00,775, together with the appropriate depreciation for the current year calculated upon the same principles as those adopted in the case of the other company. The profits and allowances having been ascertained in this way, the appellants contended that the lesser sum, *i.e.*, profits, should be deducted from the greater, *i.e.*, the unabsorbed depreciation allowance, and the resultant figure carried forward to the next year, the appellant being thus entitled to the future benefit of both sets of unabsorbed depreciation allowance as a deduction from its future profits.

The respondent, on the other hand, asserted that the correct method to adopt was to find the profits of the Bengal Company for the 8 months from the 1st April to the 2nd December, 1936, and to deduct the resultant figure from the unabsorbed depreciation allowance standing to the credit of that company on the 1st April, 1936, together with the further proper depreciation to be allowed to that company for the same 8 months, calculated on the original cost of those assets to that company. This calculation admittedly would result in a minus figure, but, said the income-tax officials, no further benefit of this unabsorbed depreciation was to be given to anyone.

So far as the Indian Company was concerned, it was to enjoy the advantage of

(1) depreciation allowance for the whole year in respect of its original buildings, etc., calculated on the cost of those assets to it,

(2) depreciation allowance for the period 3rd December, 1936, to 31st March, 1937, on the assets acquired from the Bengal Company, calculated not on the cost to that company, but on the price at which the Indian Company acquired them from that company, and

(3) its own unabsorbed allowance carried forward from the beginning of the fiscal year.

From these three sums added together was to be deducted the profits of the business—meaning thereby the profits of the Indian Company (if any) for the whole year, together with those of the acquired business for the period 3rd December, 1936, to 31st March, 1937. The resultant sums would still be a minus quantity and would remain as an unabsorbed depreciation allowance to the credit of the Indian Company, but the benefit of the unabsorbed balance of the other company could not be used to diminish future income-tax returns of the Indian Company.

The contentions of each party as applicable to the present case can be set out with substantial accuracy by quoting from the figures in the stated case.

The company in their return claimed the following sums as admissible by way of depreciation :

| | | | | |
|------------------------------------------------------------|-----|-------------|---|---|
| (a) Depreciation of the two companies for the year 1936-37 | ... | 23,49,815 | 0 | 0 |
| (b) Unabsorbed depreciation of the Indian Company | ... | 62,00,775 | 0 | 0 |
| (c) Unabsorbed depreciation of the Bengal Company | ... | 85,69,148 | 0 | 0 |
| Total | | 1,71,19,738 | 0 | 0 |

The Appellate Assistant Commissioner's conclusions were as follows :—

(i) *Bengal Iron Company.*

| | | | | |
|------------------------------------------------------------------------------------------------------------------------------------------------|-----|----------|---|---|
| (a) Depreciation allowance in respect of the original property of the Bengal Company for 8 months from the 1st April to the 2nd December, 1936 | ... | 8,62,329 | 0 | 0 |
|------------------------------------------------------------------------------------------------------------------------------------------------|-----|----------|---|---|

| | | | | |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------|---------|-----------|-----------|-----|
| (b) Unabsorbed allowance as above | ... | 85,45,150 | 0 | 0 |
| | Total | ... | 94,07,479 | 0 0 |
| Less profits of the business for this period. | | | 8,76,162 | 0 0 |
| Depreciation allowance left unabsorbed | ... | 90,81,317 | 0 | 0 |
| <i>(ii) Indian Iron and Steel Company.</i> | | | | |
| (a) Depreciation allowed in respect of the original property of the Indian Company for the year 1936-37 | ... | 7,60,077 | 0 | 0 |
| (b) Depreciation allowance in respect of the property acquired from the Bengal Company for the period 3rd December, 1936, to the 31st March, 1937 | ... | 3,77,767 | 0 | 0 |
| (c) Unabsorbed depreciation allowance as above | ... | 62,00,775 | 0 | 0 |
| | * Total | ... | 73,38,619 | 0 0 |
| Less profits of the original business for the fiscal year, together with that of the acquired business for the period 3rd December 1936, to 31st March 1937 | ... | 36,54,295 | 0 | 0 |
| Depreciation allowance left unabsorbed | ... | 86,84,824 | 0 | 0 |

In the figures of the appellant's claim the sum of 23,49,815-0-0 was calculated upon the original cost to the Indian Company of its own assets and the original cost to the Bengal Company of the assets taken over from it.

On the other hand, the figure of 3,77,767-0-0 in the Assistant Commissioner's calculation was based upon the cost to the Indian Company of the assets which it took over from the Bengal Company.

This difference of computation is a further but subsidiary matter of contention between the parties and is best dealt with in considering the major dispute.

The argument on behalf of the appellant was, as their Lordships understood, it, put in the following way :

At the beginning of the year the Bengal Company was entitled to an unabsorbed depreciation allowance of Rs. 85,45,150. If it had carried on business until the end of the year it would have been entitled to the benefit of this sum, together with the appropriate depreciation for the current year calculated upon the original cost of the assets. Then, it was said, Section 26 (2) provides that the assessment is to be made on a person succeeding to the business as if he had been carrying it on

throughout the previous year and had received the whole of the profits for that year.

The Indian Company, it was argued was the successor and was to be assessed as if it had carried on the Bengal Company's business for the whole year, though in fact it had only carried it on for 4 months. If it had carried that business on for the whole year it would have been entitled to the allowances claimed, and "as full effect could not be given to those allowances" because they exceeded the profits, then, under proviso (b) to Section 10 (2) (vi), that part of the allowance to which effect had not been given should be added to the amount of depreciation of the combined business for the following year and, it is added, so on for succeeding year subject to the limitation contained in proviso (c).

It is true, as the appellant admits, that the allowance is only to be made in respect of the property of the assessee; that the Indian Company was the assessee, and, strictly speaking, the assets of the Bengal Company only became the property of the Indian Company from the 3rd December, 1936.

But "assessee," the Company maintained, must be read distributively as meaning the owner of the property for the time being, *i.e.*, the assessee or his predecessor, as the case may be. In support of this contention they point out that such a construction is necessary in other parts of the sub-section, *e.g.*, in sub-section (2) (i) and (ii). The words "used as a dwelling house by the assessee" must refer to the assessee or his predecessor, or to both in cases where each is owner of the property for part of the fiscal year. So too in sub-*paras* (vii) and (vii-a). Unless "assessee" includes predecessor no depreciation could be claimed in respect of the period during which the predecessor still owned the property and the successor had not acquired it.

There is no doubt truth in the contention that the word "assessee" in Section 10 (2) must, when there is a successor to the business charged to tax, be read in certain of the paragraphs as including both predecessor and successor, but their Lordships are not prepared to assent to the argument that it follows as a consequence that the unabsorbed depreciation allowance of the predecessor must be added to that of the successor or to agree that even in a case when the only business concerned is that which is transferred, the business when transferred carries to the purchaser its unabsorbed allowance. Indian income-tax is assessed and paid in the next succeeding year upon the results of the year before. If then Company A sold its business to Company B in the first of the two years, apart from the provisions of

Section 26 (2), the former company could not be assessed and would not be liable for any profits it then made, because it would not be carrying on the business in the next year for which in the normal course the assessment would be made and in respect of which tax would be due, nor would Company B be liable except for any period during which it had itself owned the business and made profits, because the tax under Section 10 (1) is only "payable by an assessee under the head 'business' in respect of the profits or gains of any business carried on by him."

To meet this contingency, whether in the case of a company or an individually owned business, Section 26 was passed, and it is concerned not with the computation of tax, but with the person upon whom the liability is imposed. When, but not until, the person to pay has been ascertained do the terms of Section 10 become material in order to discover how the amount to be paid is to be computed. If this be the true method of approach, the Indian Company no doubt is liable as assessee as if it had been carrying on the Bengal Company's business throughout the previous year and had received the whole of the profits for that year. But this only means that the profits of the Bengal Company are to be ascertained in accordance with the provisions of Section 10 for the period during which it carried on the business, and that the profits of the Indian Company are to be ascertained for the period during which it carried on that business in accordance with the same principles. Whether the latter are calculated upon the earnings of the combined business or separately for each part of it, the resultant figure, when added to the Bengal Company's profits (if any), will cause the Indian Company to be assessed as if it had carried on the Bengal Company's business for the whole year. It is itself liable for the last 4 months, and by the addition of liability for the previous 8 months it will be assessed as if it had been carrying on the business throughout the year.

The object is to impose liability for the whole profits, and in finding out what they are, the actual circumstances have to be considered.

So far there is nothing to suggest that once the Bengal Company has ceased to carry on business its unabsorbed depreciation allowance should be carried on for the benefit of the Indian Company.

But it is said that company is to be treated as if it had been carrying on the business throughout the year: in that year full effect could not be given to its depreciation allowance, whether unabsorbed in previous years or acquired in the year in question, and under the direct terms of proviso (b), this allowance is to be added to that for the

following year and to be deemed to be part of that allowance, and so on for succeeding years.

To the answer that what is given is "such allowance" only and "such allowance" when read together with the previous language of sub-section (2) (vi) can mean only an allowance in respect of depreciation of buildings, etc., being the property of the assessee, it is replied that "assessee" in this as in the other sub-sections previously referred to includes predecessor as well as successor, and that the proviso in conjunction with Section 26 should be read as saying: "Where full effect cannot be given in any year to the allowance proper to be given to the assessee or to his predecessors or to both, the allowance or the unused part thereof shall be added to the amount of the allowance to which the assessee is entitled for the following year."

Their Lordships see no reason for giving this wide meaning to the word "assessee" in the proviso to Section 10 (2) (vi).

Under the definition in Section 2 (2) "Unless there is anything repugnant in the subject or context... 'assessee' means a person by whom income-tax is payable" and in the view of the Board there is nothing repugnant in the subject or context to prevent this definition being applicable to para. (vi).

Moreover, the allowance, in addition to being given in respect of the depreciation of buildings, etc., being the property of the assessee, is to be calculated on the original cost to the assessee. If "cost to the assessee" may mean either cost to the predecessor or cost to the successor, on what cost is the depreciation to be calculated when the property passes from one to the other in the course of the fiscal year?

There may well be good ground for holding that cost to the assessee means cost to the predecessor so long as he continues to be owner of the property. Indeed, it was so held in *Commissioner of Income-tax v. Masagaon Dock, Ltd.*¹

But once the property has passed to the successor, he is the assessee, the depreciation is, in the words of the Act, to be calculated on the cost to him, and there is in their Lordships' opinion no reason for holding that the cost to the predecessor is thereafter to be adopted as the basis of depreciation. This view is in accordance with that expressed in *Commissioner of Income-tax v. Buckingham & Carnatic Co. Ltd.*² It is true that in both the cases referred to above the transfer took place at the end of one fiscal year and the beginning of the next, and therefore neither case is a direct authority on the question now before the Board. But the principles are similar, and as their Lordships think, show the method upon which the computation is to be

(1) (1938) I.L.R. 1938 Bom. 374; 5 I.T.R. 124.

(2) (1935) L.R. 63 I.A. 74; 3 I.T.R. 384.

made. They are in agreement with the view of Mr. Justice Panckridge in the High Court in Calcutta in considering that if and in so far as *Re Kamalapat Motilal*¹ lays down any different principles it is wrong.

The argument on behalf of the appellant can perhaps be most strongly put by postulating the sale at the end of the fiscal year of a business carried on by a company or individual to another individual not previously carrying on any business or to a company formed solely for the purpose of carrying it on. If the business had not been sold it would have continued to enjoy the benefit of any unabsorbed depreciation allowance. Why, it is said, should it lose that benefit because it has changed hands?

No doubt the example given does indicate a case in which some hardship may be said to arise, but the object of Section 10 is not to bolster up unsuccessful businesses, it is merely to protect them, in the hands of those who find the capital, against undue taxation. The example may be countered by quoting a case in which a bankrupt business with a large unabsorbed depreciation allowance is bought by a flourishing house in order to enhance its own allowance and decrease its taxation. Success in the latter circumstances would be at least as undesirable as failure in the former is unfortunate. But in any case, the matter must depend on the wording of the section, and not upon the consequences which follow.

Their Lordships desire to refer to two more matters raised in argument.

(1) The appellant in its case placed some reliance upon the assignment to them in the agreement of the 8th September, 1936, by the Bengal Company of "the benefit, so far as capable of being assigned, of any claim which the Bengal Company may have in respect of unabsorbed depreciation allowances." It was, however, admitted before the Board that these allowances were unassignable in law and it is therefore unnecessary for their Lordships to express any opinion upon the question.

(2) Those representing the respondent took the point, but without pressing it, that the claim of the appellant was prematurely brought. It was said, as was the fact, that the case now the subject of appeal was stated under Section 66 (2) of the Indian Income-tax Act (1922), that that section gave the right to require a case to be stated to an "assessee" only, that even though the view most unfavourable to the appellants was taken, yet the result would still leave an unabsorbed balance in his favour; and that consequently there could be no assessment and no assessee.

Having regard to the conclusion which they have reached, their Lordships do not find themselves compelled, and indeed were not invited, to pronounce upon this argument. In the present instance, at any rate, it was obviously desirable that the appellant should ascertain its position at once and should not be compelled to wait possibly for years in order to discover what its financial position was. But the question is open to be taken by the Income-tax authorities on another occasion if they think anything is to be gained by doing so.

In the result their Lordships will humbly advise His Majesty that the appeal be dismissed. The appellant must pay the respondent's costs of the hearing before the Board.

Appeal dismissed.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME-TAX, BOMBAY

v.

EDULJI F. E. DINSHAW.

BEAUMONT, C. J., and KANIA, J.

April 7, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922 AS AMENDED IN 1939),*
SEC. 33, SEC. 34, SEC. 18—INDIAN FINANCE ACT, 1939, SEC. 6 (1) AND (4)
—SUPER-TAX CALCULATED AT LOWER RATE BY APPELLATE ASSISTANT
COMMISSIONER—WHETHER COMMISSIONER ENTITLED TO RESTORE
HIGHER RATE IN REVISION—POWERS IN REVISION, LIMITS OF—APPLI-
CABILITY OF SUPER-TAX RATES FIXED BY FINANCE ACT OF 1939 TO IN-
COME OF RESIDENTS IN BRITISH INDIA EARNED IN 1938-39—SCOPE OF
EXEMPTION FROM NEW RATES CONFERRED BY SEC. 6.

The assessee was a resident in British India and his income was mainly from dividends and securities. For the year 1939-40 the Income-tax Officer calculated the income-tax payable by the assessee at the rates prescribed in the Indian Finance Act of 1938, and calculated super-tax at the rates prescribed in the Indian Finance Act of 1939, in view of the provisions contained in Section 6 (4) (b) of the Finance Act of 1939 read with Section 18 of the Indian Income-tax Act, 1922, as amended in 1939. On appeal, the Appellate Assistant Commissioner held that super-tax also should be calculated at the rates prescribed by the Finance Act of 1938 and ordered a refund of the excess paid. The Commissioner of Income-tax in exercise of his powers of revision under Section 33 held that super-tax should be calculated under the Finance

Act of 1938 and enhanced the amount of super-tax to the figure originally fixed by the Income-tax Officer :

Held, (i) *that the Commissioner had no power under Section 33 of the Act to enhance the tax assessed by the Appellate Assistant Commissioner on the ground that income had escaped or had been assessed at too low a figure, though he could have directed the Income-tax Officer to take action under Section 34 within the time limit prescribed for initiating proceeding under that section ;*

Sheik Abdul Kadir v. Commissioner of Income-tax [1927] (2 I.T.C. 372), Commissioner of Income-tax, Burma v. Ved Nath Singh [1940] (8 I.T.R. 222) and Commissioner of Income-tax, Bombay v. Khemchand [1938] (6 I.T.R. 414) followed.

(ii) *that on a proper construction of Section 18 of the Indian Income-tax Act and Section 6 of the Indian Finance Act of 1939, super-tax on the assessee's income had to be calculated at the rates applicable for the year 1939-40 as he was a resident in British India.*

Though super-tax is merely an additional duty of income-tax for most purposes of the Income-tax Act, the Finance Act of 1939 makes a distinction between the two taxes, and 'income-tax' in Section 6 of the Finance Act of 1939 does not include super-tax.

Cases referred to :—

Commissioner of Income-tax, Bombay v. Khemchand [1938] (6 I.T.R. 414).

Commissioner of Income-tax, Burma v. Ved Nath Singh [1940] 8 (I.T.R. 222).

Sheik Abdul Kadir v. Commissioner of Income-tax, Madras [1927] (2 I.T.C. 372).

Case referred to the High Court of Bombay by the Commissioner of Income-tax, Bombay : [Income-tax Reference No. 11 of 1942].

Facts appear in the following Statement of Case made by the Commissioner.

STATEMENT OF CASE.

" My Lords,

Under Section 66 (2) of the Indian Income-tax Act, XI of 1922, (hereinafter referred to as ' the Act ') and at the instance of Mr. Edulji F. E. Dinshaw of Bombay (hereinafter referred to as ' the assessee '), I have the honour to refer for your Lordships' decision certain questions which have arisen out of the assessment of the assessee for the financial year 1939-40.

2. **Facts of the case.**—The assessee is a resident of Bombay. For the year 1939-40 he was assessed on a total income of Rs. 3,60,580 derived from the following sources :

| | Rs. |
|------------------------|--------------|
| Dividends | ... 2,03,790 |
| Interest on securities | ... 1,27,845 |

| | | |
|-------------------------------------|-----|----------|
| Property | ... | 22,957 |
| Shares from Messrs. Payne & Co. | ... | 5,188 |
| Bank interest and other minor items | ... | 800 |
| | | <hr/> |
| | | 3,60,580 |
| | | <hr/> |

Under sub-section (4) of Section 6 of the Indian Finance Act, 1939, the Income-tax Officer calculated the income-tax payable on this income at the rates prescribed in the Indian Finance Act, 1938, but he calculated the super-tax at the rates prescribed in the Indian Finance Act, 1939. A copy of the assessment order is annexed and marked A.

3. The assessee appealed to the Appellate Assistant Commissioner against the Income-tax Officer's decision with regard to super-tax and the Appellate Assistant Commissioner held that super-tax as well as income-tax should be calculated at the rates prescribed in the Indian Finance Act, 1938. A copy of his order is annexed and marked B. In accordance with this order a refund of super-tax was sanctioned and the assessee actually received the refund on the 8th of March, 1940.

4. On the 5th of August, 1940, my predecessor issued a notice to the assessee under Section 33 of the Act, stating that it appeared to him that the Appellate Assistant Commissioner had incorrectly reduced the super-tax assessment and calling upon the assessee to show cause why the Income-tax Officer's order should not be restored. The assessee's representative appeared in compliance with this notice and my predecessor passed an order cancelling the reduction granted by the Appellate Assistant Commissioner and restoring the original demand in respect of super-tax. A copy of this order is annexed and marked C.

5. **Questions for decision.**—Being dissatisfied with the order passed by my predecessor the assessee filed an application (copy annexed and marked D) for a reference to the High Court under Section 66 (2) of the Act on the following questions :—

(1) Whether the Commissioner can revise the order of the Appellate Assistant Commissioner under Section 33 and ask the assessee to repay the amount of the refund ordered by the Assistant Commissioner after the Appellate Assistant Commissioner's order to make the refund has been carried out and the amount of refund has been received by the assessee.

(2) Whether, on a proper construction of the Indian Income-tax Act and of the Indian Finance Act, 1939, the super-tax ought not to be charged to the assessee at the rates applicable for the year beginning 1st April 1938.

I agree that these are questions of law which arise from my predecessor's order and I accordingly refer them for your Lordships' decision.

6. Opinion of the Commissioner.—Under Section 33 of the Income-tax Act as it stood at the time of my predecessor's order the Commissioner had power to call for the record of any proceedings under the Act which had been taken by any authority subordinate to him and to pass such order thereon as he might think fit. It was further provided that he should not pass any order prejudicial to the assessee without hearing him or giving him a reasonable opportunity of being heard. The proviso makes it clear that the Commissioner had power to pass a prejudicial order and it is obvious that such an order may involve an enhancement of the tax payable by the assessee. The Commissioner's powers were not restricted except by the words "subject to the provisions of this Act." In the case of *Khemchand Ramdas*¹ the Privy Council held that the Commissioner could not direct an Income-tax Officer to issue a supplementary demand after the expiry of the time limits prescribed by Sections 34 and 35, but in the present case action was taken well within those limits. The fact that a refund had previously been granted on the basis of the Appellate Assistant Commissioner's order does not affect the powers of the Commissioner in any way. The Income-tax Officer was bound to grant a refund in accordance with the order passed by the Appellate Assistant Commissioner and he was equally bound to levy an additional demand in accordance with an order passed by the Commissioner. As has already been stated the assessee was given an opportunity of being heard, as required by the proviso, before the Commissioner's order was passed. In these circumstances I can see no reason for holding that my predecessor exceeded his powers and I respectfully submit that the answer to the first question should be in the affirmative.

7. As regards the second question I reproduce below for facility of reference, sub-section (4) of Section 6 of the Indian Finance Act, 1939 :

"(4) Notwithstanding anything contained in sub-section (1) or sub-section (2), where more than half of the total income of any individual or Hindu undivided family consists of income from salaries, interest on securities or dividends in respect of which the individual or Hindu undivided family is deemed, under the provisions of Section 49-B of the Indian Income-tax Act, 1922, to have paid income-tax imposed in British India, or consists of income falling under more than one of those heads :

(a) income-tax for the year beginning on the 1st day of April 1939 shall be charged in respect of such total incomes at the rates of

(1) (1938) 6 I.T.R. 414.

income-tax which were imposed for the year beginning on the 1st day of April 1938 in respect of incomes of individuals or Hindu undivided families, and

(b) in cases in which super-tax has been deducted under provisions of Section 18 of the said Act or would have been so deductible had the Indian Income-tax (Amendment) Act, 1939, come into force on the 1st day of April 1938, the rates of super-tax for the year beginning on the 1st day of April 1939 shall, for the purposes of Section 55 of the Indian Income-tax Act, 1922, be the rates of super-tax which were imposed for the year beginning on the 1st day of April 1938 in respect of incomes of individuals or Hindu undivided families, as the case may be."

The assessee claims that clause (a) of this sub-section applies to super-tax as well as income-tax. It is true that Section 55 of the Act defines super-tax as "an additional duty of income-tax" and Section 58 provides that unless otherwise specified all the provisions of the Act relating to the charge, assessment, collection and recovery of income-tax shall apply also, so far as may be, to the charge, assessment, collection and recovery of super-tax. These provisions however have no application to the Indian Finance Act, which prescribes the rates at which each tax is to be imposed during the ensuing year. The Indian Finance Act makes a clear distinction between income-tax and super-tax and contains no provision on the strength of which it can be contended that "income-tax" should be regarded as including super-tax. In the absence of any such provisions, clause (a) of the sub-section quoted above is in my opinion applicable only to income-tax as distinct from super-tax.

8. If clause (b) and not clause (a) is applicable to super-tax, the old rates of super-tax cannot be applied in any assessment unless:

(1) more than half of the total income consists of salaries, interest on securities or dividends, and

(2) super-tax has been deducted under the provisions of Section 18 of the Income-tax Act or would have been so deductible had the Indian Income-tax (Amendment) Act, 1939, come into force on the 1st day of April 1938.

In the present case the first condition is admittedly satisfied but the second condition is not satisfied since Section 18, as amended by the Income-tax (Amendment) Act, 1939, provides for the deduction of super-tax at source only in the case of income chargeable under the head "salaries" and in the case of income from securities and dividends payable to non-residents. As the assessee is resident in British India and has no income chargeable under the head "salaries" super-tax

would not have been deductible at sources in his case even if the Income-tax (Amendment) Act, 1939, had come into force from the 1st April 1938.

9. For the above reasons I am respectfully of opinion that the answer to the second question should be that super-tax has been correctly charged at the rates applicable for the year beginning on the 1st day of April 1939."

Sir Jamsheedji Kanga with *B. J. Kolah*, for the assessee.

M. C. Setalvad with *G. N. Joshi*, for the Commissioner.

JUDGMENT.

BEAUMONT, C. J.—This is a reference by the Income-tax Commissioner raising two questions, which arise in the following circumstances. The assessment year was the year 1939-40, and the accounting year was from April 1, 1938, to March 31, 1939. On December 22, 1939, the Income-tax Officer made his assessment, and it is apparent from the figures given in the case that more than half of the income of the assessee was derived from dividends and interest on securities. Under sub-section (4) of Section 6 of the Finance Act of 1939 the Income-tax Officer calculated the income-tax payable at the rates prescribed in the Finance Act of 1938, but he calculated the super-tax at the rates prescribed in the Finance Act of 1939. The assessee appealed to the Appellate Assistant Commissioner against the assessment, and the Appellate Assistant Commissioner, who was Mr. Murphy, held that super-tax, as well as income-tax, ought to have been calculated at the rates prescribed in the Finance Act of 1938. In accordance with his order a refund of super-tax was sanctioned, and the assessee received the refund in March, 1940. In August, 1940, Mr. Murphy, who had then become the Commissioner, issued a notice to the assessee under Section 33 of the Indian Income-tax Act, stating that it appeared to him that the Appellate Assistant Commissioner, who was Mr. Murphy himself, had incorrectly reduced the super-tax assessment, and calling upon the assessee to show cause why the Income-tax Officer's order should not be restored. On the hearing of that notice the Commissioner took a different view to that which he had taken as Appellate Assistant Commissioner, and directed that the super-tax demand be enhanced to the figure at which it had originally been assessed by the Income-tax Officer.

The two questions which, in substance, arise, are, first, whether the Income-tax Commissioner had power under Section 33 to make the order which he did make; and, secondly, if he had such power, whether the order he made was right. The first question depends

entirely on the construction of the Income-tax Act, as it existed on the material dates. The assessment was made under Section 23 and under Section 29 notice of demand was served. The demand was complied with, and the tax was paid. Under Section 30 the assessee had a right to appeal to the Appellate Assistant Commissioner, which right he exercised, with the result which I have already stated. Under Section 32 he had a further right of appeal, if he so desired, to the Commissioner. Then comes Section 33, which provides that the Commissioner may of his own motion call for the record of any proceeding under the Act which has been taken by any authority subordinate to him or by himself when exercising the powers of an Appellate Assistant Commissioner under sub-section (5) of Section 5, and on receipt of the record the Commissioner may make such inquiry or cause such inquiry to be made and, subject to the provisions of the Act, may pass such order as he thinks fit. Then Section 34 provides for the income of an assessee having escaped assessment, and, so far as material, provides that if for any reason income chargeable to income-tax has escaped assessment in any year, or has been assessed at too low a rate, the Income-tax Officer may, at any time within one year of the end of that year, serve on the person liable to pay tax on such income a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of Section 22, and may proceed to assess or reassess such income, and the provisions of the Act, so far as may be, apply accordingly as if the notice were a notice under that sub-section. So that the scheme under Section 34 is that if the Income-tax Officer considers that income has escaped assessment, he serves a notice corresponding to the notice which he would serve for making the original assessment, and then he proceeds to make a fresh assessment, and the assessee would have the same right of appeal against that fresh assessment as he had against the original assessment. In my opinion, it is clear that the Commissioner of Income-tax cannot by a revision order under Section 33 enhance the tax on the ground that income has escaped assessment, unless he proceeds under Section 34. He can, no doubt, under Section 33 direct the Income-tax Officer to take action under Section 34; but, in my opinion, if a re-assessment is to be made on the ground that income has escaped assessment, that can only be done by the procedure laid down under Section 34.

The argument of the Commissioner seems to me to produce most extraordinary results. His contention is that under Section 33 he can call for the papers before the Income-tax Officer, at any rate within the time limited by Section 34, and he can then of his own motion

enhance the assessment on the ground that income has escaped assessment, or been assessed at too low a rate. It is argued that there was not an enhancement of the tax, because the amount was restored to the figure at which the Income-tax Officer had originally assessed it. But, in my opinion, if the Commissioner was entitled to enhance the assessment, as it existed under the appellate order of the Assistant Commissioner, he could have enhanced it to any amount, not only to the amount at which it had been assessed by the Income-tax Officer. At the time when the Commissioner took action under Section 33 the assessment was that which had been arrived at as a result of the Appellate Assistant Commissioner's order, and, in my judgment, the Commissioner had no power to increase that amount on the ground that income had escaped assessment, or been assessed at too low a figure, except by directing the Income-tax Officer to proceed under Section 34. That view is in accordance with the views expressed by two High Courts, the Madras High Court in *Sheik Abdual Kadir v. Commissioner of Income-tax*¹, and by the Rangoon High Court in *Commissioner of Income-tax, Burma v. Ved Nath Singh*².

The Commissioner in this case expressed the opinion that the action of his predecessor was justified. The Commissioner is required under Section 66 (2) to state his opinion, and not merely to argue the case which his office desires to set up. That can be left to counsel at the hearing. I must confess I think it unfortunate that the Commissioner in stating his opinion did not think fit to refer to the decisions of the two High Courts, of which he can hardly have been ignorant, and which appear to me to be inconsistent with the opinion which he expressed. He does not notice the difficulty that to employ the power of revision under Section 33 to enhance the assessment on the ground that income has escaped assessment would be to enable that operation to be performed without the safeguards which are provided by Section 34, namely, that there must be a fresh assessment from which the assessee would have a right of appeal under the Act. It was pointed out by Mr. Setalvad that the right of appeal was only to the Assistant Commissioner and to the Commissioner, and, no doubt, in practice that right of appeal proved a farce. I have been hearing income-tax references in this Presidency for the last thirteen years, and I would say that in at least ninety per cent. of the cases which have come before this Court the Assistant Commissioner has agreed with the Income-tax Officer, and the Commissioner has agreed with the Assistant Commissioner, however complicated and difficult the questions may have been. But although that may have been the result in practice of giving a

(1) (1927) 2 I.T.C. 372. (2) (1940) 8 I.T.R. 222.

right of appeal to superior Income-tax Officers, I apprehend that that was not what was in the contemplation of the Legislature when they gave the right of appeal. I have no doubt they contemplated that superior officers would exercise their powers in a judicial spirit, and consider on merits the cases which came before them. It seems to me quite impossible to suppose that the Legislature intended that the rights of appeal which were given could be overridden by the Commissioner exercising his powers of revision under Section 33. Section 33 only enables the Commissioner to make an order, subject to the provisions of the Act, and I think the decision of the Privy Council, to which we have been referred, in *Commissioner of Income-tax, Bombay v. Khemchand*¹, supports the view that those words prevent the Commissioner from making an order under Section 33, which would fall under Section 34 or Section 35.

The actual question raised is in a curiously limited form. The question asked is :

“ Whether the Commissioner can revise the order of the Appellate Assistant Commissioner under Section 33 and ask the assessee to repay the amount of the refund ordered by the Assistant Commissioner after the Appellate Assistant Commissioner's order to make the refund has been carried out and the amount of refund has been received by the assessee ? ”

It seems to me that the answer to that question necessarily involves the consideration of the wider question whether the Commissioner can under Section 33 revise an assessment by holding that income has escaped assessment, and I have no doubt whatever that the answer to the question must be in the negative.

The second question is :

“ Whether on a proper construction of the Indian Income-tax Act and of the Indian Finance Act, 1939, the super-tax ought not to be charged to the assessee at the rates applicable for the year beginning April 1, 1938.”

If our answer to the first question is correct, the second question does not, of course, arise. But as this case may go further, I think it desirable to express an opinion on that second question, which seems to me to present no great difficulty. The question turns entirely on the construction of Section 6 of the Finance Act of 1939. That section provides in sub-section (1) :

“ Subject to the provisions of sub-section (2)

(a) income-tax for the year beginning on the 1st day of April, 1939, shall be charged at the rates specified in Part I of Schedule II, and

(1) (1938) 6 I.T.R. 414.

(b) rates of super-tax for the year beginning on the 1st day of April, 1939, shall, for the purposes of Section 55 of the Indian Income-tax Act, 1922, be those specified in Part II of Schedule II."

Then comes sub-section (4) which creates the only difficulty. That sub-section provides :

"Notwithstanding anything contained in sub-section (1) or sub-section (2), where more than half of the total income of any individual or Hindu undivided family consists of income from salaries, interest on securities or dividends in respect of which the individual or Hindu undivided family is deemed, under the provisions of Section 49B of the Indian Income-tax Act, 1922, to have income-tax imposed in British India, or consists of income falling under more than one of those heads—

(a) income-tax for the year beginning on the 1st day of April, 1939, shall be charged in respect of such total incomes at the rates of income-tax which were imposed for the year beginning on the 1st day of April, 1938, in respect of incomes of individuals or Hindu undivided families,..."

Pausing there for a moment, it is not disputed that the assessee falls within the class specified in sub-section (4) and so far as income-tax is concerned, his tax has been assessed at the rates applicable for the year 1938. But then comes sub-clause (b), which provides that—

"in cases in which super-tax has been deducted under the provisions of Section 18 of the said Act or would have been so deductible had the Indian Income-tax (Amendment) Act, 1939, come into force on the 1st day of April, 1938, the rates of super-tax for the year beginning on the 1st day of April, 1939, shall, for the purposes of Section 55 of the Indian Income-tax Act, 1922, be the rates of super-tax which were imposed for the year beginning on the 1st day of April, 1938, in respect of incomes of individuals or Hindu undivided families, as the case may be."

Now, it is admitted that the assessee, being a resident in India, does not fall within the terms of sub-clause (b), because the tax would not have been deductible under Section 18, and that seems to me to dispose of the matter. In my view, sub-section (4) grants relief to a certain class of persons, which class includes the assessee. In the case of income-tax, relief is granted under sub-clause (a), and in the case of super-tax it is granted under sub-clause (b), and unless the assessee falls within sub-clause (b), no relief is granted to him, and he has to pay super-tax at the rates specified in Schedule II. It seems to me impossible to extract any other meaning out of the section.

The argument of the assessee is that he can either comply with the conditions in sub-section (4) limiting the class of persons to whom relief is granted, or he can comply with the terms of sub-clause (b). It seems to me obvious that if he only falls within the class no relief is granted to him in respect of super-tax unless he falls within sub-clause (b). No doubt, super-tax is merely an additional duty of income-tax for most of the purposes of the Income-tax Act, but in Section 6 of the Finance Act the two duties are distinguished. Therefore, if it is necessary to answer the question, I should answer it by saying that, on a proper construction of the Indian Finance Act, 1939, the super-tax ought to be charged to the assessee at the rates applicable for the year beginning April 1, 1939. It is difficult to answer the question by an affirmative or negative, because it is stated in a negative form.

Commissioner to pay costs.

Deposit of Rs. 100 to be refunded.

KANIA, J.—Two questions have been submitted by the Commissioner for the Court's opinion. The first question recites also whether the power under Section 33 could be exercised after an order of refund is carried out by the office. That fact in my opinion is not material. The principle involved in the question is of far-reaching effect and is not necessarily connected with the fact that the Income-tax Officer had refunded the payment on the order made by the Appellate Assistant Commissioner. The question is whether when the Commissioner purports to act under Section 33, he has the power to fix a sum for the assessment, which is higher than the sum fixed by the Appellate Assistant Commissioner, on the ground that some income had escaped assessment or the rate charged was lower than the one which should have been charged. I propose to confine my observations to that situation, because in the present case the ground for revision is stated to be that the rate charged was lower than what ought to have been charged.

On behalf of the Commissioner it was urged that Section 33 of the Act (in force at the time of the assessment) gave the Commissioner the widest powers to make such orders as he thought fit. The section is expressly worded so as to make it subject to the provisions of the Act. That expression was construed by the Privy Council in *Commissioner of Income-tax, Bombay v. Khemchand*¹ as covering Sections 34 and 35. When it was argued that the Commissioner could revise an order at any time he thought fit, Lord Romer, in the course of his judgment, observed :—

(1) (1938) 6 I.T.R. 414.

" Their Lordships would, in any case, hesitate long before acceding to a contention that would lead to so extravagant results. In their opinion, however, the contention cannot prevail. The Commissioner's powers under Section 33 can only be exercised subject to the provisions of the Act of which the provisions in Sections 34 and 35 are in this respect of the greatest importance."

Therefore the contention that the Commissioner had the wide powers as contended for is set at rest by those observations.

The next question is whether in making his order in this case the Commissioner was acting within his powers, as interpreted by the judgment of the Privy Council. I have already pointed out that the Commissioner in this case had put up the figure of super-tax beyond what the Appellate Assistant Commissioner had fixed and the only ground on which that was done was that the rate fixed by the Appellate Assistant Commissioner was lower than the one permitted by law. It should be noted that in Section 34 these are the very words used. The construction of Section 33 when read with Sections 34 and 35 was considered by the Madras High Court and the Rangoon High Court in the two cases referred to by the learned Chief Justice in his judgment and both the Courts came to the conclusion that it was not right for the Commissioner while purporting to act under Section 33 to override the provisions of Section 34. It seems to me clear that if the Commissioner thought that the view of the Appellate Assistant Commissioner was erroneous and a different view should be taken, it was his duty to give directions to proceed under Section 34 and it was not within his power himself to Act as if under Section 34 and re-assess on the ground that the rate charged was lower. The argument that the figure fixed by the Commissioner is the same has no substance, because the question is of the interpretation of the section and the Commissioner's powers under that section. If the power to re-assess and enhance the figure which was assessed by the Appellate Assistant Commissioner exists, there is no reason to think that the power is limited to putting it up only to the extent it was originally fixed by the Income-tax Officer. I therefore agree that the first question should be answered in the negative.

Under the circumstances the second question is not necessary to be answered. If necessary, I agree that it should be answered as suggested by the learned Chief Justice. It is clear that under the Indian Finance Act, 1939, by Section 6 (1) it was provided that for the financial year 1939 the rates of income-tax and super-tax should be as prescribed in the schedule to that Act. Sub-section (4) was introduced to give relief in certain cases. The first part of that sub-section defines a class of persons to whom such relief was to be given. To put it briefly

it covers persons whose income from salary, interest and dividends was more than half of the total income. Sub-section (4) (a) provides what relief was to be granted to them in respect of income-tax. Although in the general scheme of the Act income-tax may include super-tax for certain purposes, it is clear that in Section 6 of the Indian Finance Act, 1939, there is a distinction between the imposition of income-tax and super-tax. Having regard to that distinction "super-tax" cannot be included in the term "income-tax" in sub-section (4) (a). Sub-section (4) (b) provides the reliefs to be given to the same class of persons in the matter of super-tax. A plain reading of that sub-section shows that out of the class mentioned in sub-section (4) relief in respect of super-tax had to be granted only in respect of persons who were covered by the express words of that sub-section. It only included persons from whose income super-tax was deducted or deductible under Section 18 of the Act. Unless therefore the assessee came within that category sub-section (4) (b) did not apply and he could only get the relief in respect of the income-tax as provided by sub-section (4) (a). Any other construction would be completely re-writing the section which it is not the function of the Court to do. It is futile to argue that this interpretation would give rise to some invidious distinctions, because sub-section (4) itself is an exempting section which creates a class of persons in whose favour exemption is granted and thereby makes a distinction as between them and the rest of the persons liable to taxation under the Income-tax Act.

Reference answered accordingly.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS

v.

MOHANMAL CHORDIA.

SIR LIONEL LEACH, C.J., and LAKSHMANA RAO, J.

March 16, 1943.

BUSINESS—JOINT FAMILY BUSINESS—GIFT OF MONEY BY JAIN WIDOW TO SONS OF ADOPTED SON AND TO HIS WIFE—BUSINESSES STARTED WITH SUCH MONEY—WHETHER SEPARATE BUSINESS OR JOINT FAMILY BUSINESS.

S, a Hindu widow, made a gift of a business founded by her husband's father to her adopted son's widow U. In May 1918, U adopted the assessee, and gave certain sums of money by way of gift to the assessee's two sons and to the assessee's wife and they started with that money three different businesses under their respective names. The Income-tax Commissioner contended that the main business to which the

assessee had succeeded on the death of U and the three businesses carried on by the assessee's sons and by his wife were really one carried on by the joint family of which the assessee was the head. The Appellate Tribunal found that the gifts made by S and U were bona fide transactions and that they had been accepted as valid by the family.

Held, that, under the circumstances, the businesses carried on in the names of the two grandsons and daughter-in-law of U were genuine businesses and were not part of the business carried on by the assessee.

LEACH, C. J.—*It was open to the members of the family to accept the gift made by S and U as being valid and binding on them and if the assessee, the person most concerned, did not challenge the validity of the gift, it was not open to a third party to do so.*

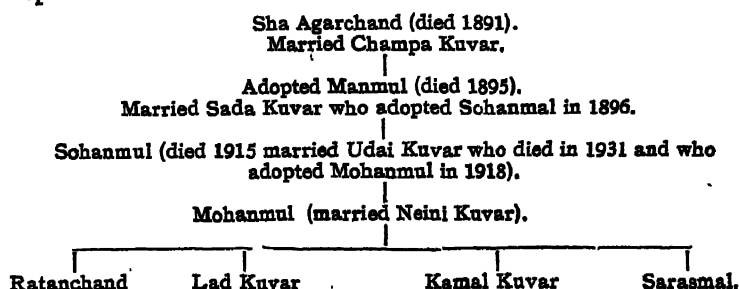
Case referred to the Madras High Court by the Income-tax Appellate Tribunal, Calcutta Bench, under Section 66 (1) of the Indian Income-tax Act, 1922. (Referred Case No. 31 of 1942).

JUDGMENT OF THE APPELLATE TRIBUNAL.

Under Section 33 of the Indian Income-tax Act (XI of 1922) the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. Varma (Judicial Member) and P. N. S. Ayyar (Accountant Member) delivered the following judgment on 10th April, 1942.

This appeal has been preferred by the Income-tax Officer, IV Circle, Madras, against the order of the Appellate Assistant Commissioner modifying the assessment made in this case. The appellant assessed the respondent as a Hindu undivided family and directed him to pay a tax of Rs. 54,990-9-0 on an income of Rs. 1,75,358. The Appellate Assistant Commissioner found the income to be Rs. 1,06,370 on the grounds which shall be considered in the other appeal against the quantum of income preferred by the respondent of this appeal. The other appeal is R.A.A. No. 29 Madras of 1941-42.

2. The admitted facts of the case will be clear by the following pedigree which will show the relationship of the present respondent with certain others whose income is sought to be assessed in his hands. The respondent is an Oswal Jain :—



Manmul, Sohanmul and Mohanmul was each in his turn adopted. Sha Agar Chand died on 12th February 1891 leaving a "will," dated the 4th February 1891. Manmul was adopted by his widow Champa Kuvar, on 26th February, 1891. He died intestate on 5th June 1895. His widow Sada Kuvar obtained letters of administration to her husband's estate on 12th August 1895. She adopted Sohanmul. There was an ante-adoption agreement dated 25th August 1896. Sohanmul was adopted by Sada Kuvar on 31st August 1896. Sohanmul also died intestate in July 1915. Sada Kuvar gifted the properties to Udai Kuvar by means of a gift deed, dated 14th April 1918. Sada Kuvar died in 1923. Udai Kuvar adopted Mohanmul in May 1918. She died in April 1931. She made gifts to her grandsons and grand-daughters in October 1930.

3. The law of adoption in relation to the Jains may be briefly set out so as to exhibit a clear conception of the case. The Jains do not believe in adoption in the same manner as the Hindus. Adoption among the Jains lacks spiritual element and is secular in character as the Jains do not perform such ceremonies after death as the Hindus do. The law of adoption is also slightly at variance with the Hindu Law in several particulars. For instance, a Jain widow can adopt without the permission of her husband or his kinsmen, while a Hindu widow requires such a permission. It is not necessary that the boy to be adopted should be unmarried. No religious ceremonies are necessary nor is there any restriction regarding the age of the adoptee. Relations prohibited for adoption amongst the Hindus are not prohibited from adoption among the Jains. The following are the case law :—

*Lakshmi Chand v. Gatto Bai*¹ : "It is true that the powers of a Jain widow in the matter of adoption are of an exceptional character, namely, that she can make an adoption without the permission of her husband or the consent of his heirs and that she may adopt a daughter's son; and further that no ceremonies or forms are necessary. But, except in these respects it is not controlled by the Hindu Law of adoption, we think that in all others its principles and rules are applicable."

*Askarfi Kunwar v. Rup Chand*² : "They find that it has been held that the ordinary Hindu Law of inheritance is applicable to Jains in the absence of proof of special customs and usages varying that law and the same rule has been applied in matters of adoption although the reasoning on which the law is based is not wholly applicable to Jains as no spiritual efficacy is attached in their case of adoption."

It is, therefore, evident that Jains are governed by the Hindu Law of inheritance and of adoption except in so far as these laws are varied in certain particulars due to special customs and usages.

(1) (1885) 8 All. 319, at 321.

(2) (1908) 30 All. 197, at 201.

4. We are concerned with the assessment of Mohanmul Chordia, proprietor Sha Agarchand Manmul. The Income-tax Officer has taken the income of Messrs. Ratanchand, Parasmal, Bai Neini Kuvar and "Ratanchand Khivraj" as income of the respondent constituting a joint family. Sha Agarchand, the earliest member of this family, so far as we are concerned, died on 18th February 1891 leaving a "will," dated 4th February 1891. His widow, Champa Kuvar, adopted Manmul on 26th February 1891. He died intestate on 5th June 1851 and his widow, Sada Kuvar, obtained letters of administration to her husband's estate on 12th August 1895. Sada Kuvar adopted Sohanmul on 31st August 1896. There was an agreement dated the 25th August 1896, executed between Sohanmul's natural father and Sada Kuvar. This agreement will have a good deal of bearing on the decision of this case. It may also be mentioned that the age of this boy was then 17 years and 8 months and he was, in law, a minor. The agreement sets out certain dispositions already made by Sada Kuvar before the adoption. We are not concerned with these dispositions as they are valid in law and not challenged by any party. The agreement recites that the business of Sha Agarchand Manmul should be continued as usual and sets out details regarding establishment, customary alms, etc. The important paragraph is paragraph (9) by which a sum of Rs. 50,000 was reserved for the adoptive mother, Sada Kuvar. It is not altogether clear from the trend of the agreement whether the whole sum was to be the absolute property of the adoptive mother, for there are restrictions restraining her from dealing with these funds as she liked. It is provided that she could on a requisition in writing by her, draw from this fund a sum not exceeding Rs. 10,000 and further she was at liberty to bequeath by "will" or give by gift a sum not exceeding Rs. 10,000. As regards the balance of Rs. 30,000 she was given no disposing power. The balance in fact was to go to Sohanmul if he were alive or to his male issue. A point worth nothing with regards to this part of the agreement is that in case Sohanmul predeceased Sada Kuvar without leaving a male issue then only was she entitled absolutely to the balance of the fund.

Paragraphs 10 to 13 of the agreement deal with certain dispositions made before the adoption with which as pointed out above, we are here concerned.

Paragraph 14 deals with certain charities.

Paragraph 15 places a limitation on the rights of the adopted son, who in the ordinary course of law, should acquire all the rights of a natural born son of Manmul. This clause further provides that the adoptive mother, *i.e.*, Sada Kuvar, should be considered to be the sole owner of the entire property and that the adopted son should have no right. We will later on consider whether this condition is valid or

whether it is repugnant to Hindu Law and whether the Hindu Law governs this case. But to continue with the facts of this case, the Income-tax Officer did not consider that an agreement of this nature was binding and held that Sohanmul on adoption divested his adoptive mother, Sada Kuvar, of the entire property less reasonable dispositions and became the owner thereof. He also held that when on the death of Sohanmul his widow, Udai Kuvar, adopted the present respondent, he became the owner of this property and together with his sons who are set out in the pedigree, formed a joint Hindu family. The assessment was made on this joint family on the entire income.

5. The Appellate Assistant Commissioner, however, took a different view and he came to the conclusion that Mohanmul Chordia is to be assessed as an "Individual," *i.e.*, in the manner in which he had submitted his return and has set aside this part of the order of the Income-tax Officer. His reasons will be made clear by the contentions which have been urged before us and they are the following :—

(i) The Jains are not governed by the Hindu Law.

(ii) When Sada Kuvar took the estate of her husband, Manmul, she took it as her absolute property. When she adopted Sohanmul, the adoption did not divest her and she continued to be the absolute owner of the properties.

(iii) There is the ante-adoption agreement dated 25th August 1896 which clearly stated that Sada Kuvar was the absolute owner of the property and that if her adopted son predeceased her she was entitled to that property. This agreement was not void or voidable and Sohanmul ratified it after coming of age as could be judged by his later conduct.

(iv) Being an absolute owner of the property she had every right to give it as a gift to her daughter-in-law, Udai Kuvar, in 1918.

(v) Udai Kuvar was the owner of the property till her death in April 1931. In October 1930 out of a total capital of about Rs.10,64,000 she gifted rupees four lakhs to her two grandsons and daughter-in-law.

(vi) Sohanmul, during his lifetime, and Mohanmul from the date of his adoption up to the date of his mother's death accepted the position that Sada Kuvar and Udai Kuvar were each in their turn the absolute owners of the property.

(vii) This position has been accepted by the Department as well as the parties themselves. The Income-tax Officer cannot now say that such and such person was not the owner and that such and such person would be deemed to be the owner and that that person had no right to act as he or she did.

(viii) The fact of gifts having been entered in the books, the Income-tax Officer cannot go against the evidence furnished by the books and disturb the position which the parties themselves have accepted between themselves. The property belonging to Neini Kuvar cannot now be ascribed by the Income-tax Officer to Mohanmul or to the estate as a whole.

The questions are intricate and are by no means easy of solution. We shall take up each of these points one by one and after dealing with them state the result.

6. Question (i):—*Are the Jains governed by the Hindu Law?*

It has been held in *Asharfi Kunwar v. Rup Chand*¹ on the authority of previous decisions that the Hindu Law of Inheritance is applicable to Jains in the absence of proof of special customs and usages varying that law. Reliance is placed in this case on 6 Indian Appeals, page 15, in the case of *Chotay v. Chunno Lall*. We are concerned with the consideration of a case of inheritance by a Jain and the above decision provides an answer to this question. The other matters will be dealt with under the appropriate headings.

7. Questions (ii):—*Absolute ownership and divesting of estate by adoption*: It is true that a sonless Jain widow succeeds to the property of her husband and takes the property absolutely. This is the variation from the ordinary Hindu Law which has been established by many decided cases. The second question which arises is to the effect of adoption and whether there was divesting of the estate or whether the widow continued to be the absolute owner of the property. The question has been dealt with partly in answer to the first argument that the ordinary Hindu Law will be held applicable to the case of Jains. But there is some distinction with regard to this point between the ordinary Hindu Law and the Jain Law, if we may use that expression. In the ordinary Hindu Law a widow acquires only a limited or a life interest, as it is called, in the property of her husband. The case is, however, different in the case of sonless Jain widows. They take an absolute interest in the property left by their husbands. The adopted son, however, divests the adoptive mother of the properties held hitherto by her even as absolute owner. This matter has been the subject matter of judicial decisions and we will merely quote some of the cases without discussing further.

8. The earliest case is that decided by their Lordships of the Privy Council in 1 Allahabad 688, in the case of *Sheosing v. Dakho Morarilal*. At page 704 Sir Montague E. Smith, who delivered the judgment, observed as follows:—

(1) (1908) 30 All. 197, at p. 202.

These findings are thus stated in the judgment, and their Lordships entirely concur in them:

"Contrasting this evidence with that given by the independent witnesses examined under the several commissions and having regard to the position which several of the Delhi witnesses hold as expounders of the law of the sect, it cannot be doubted that the weight of the evidence greatly preponderates in favour of the respondents. It appears to us that, so far as usage in this country ordinarily admits of proof, it has been established that a sonless widow of a Saraogi Agarwala takes by the custom of the sect a very much larger dominion over the estate of her husband than is conceded by Hindu Law to the widows of orthodox Hindus; that she takes an absolute interest at least in the self-acquired property of her husband (and as we have said, it is not necessary for us to go further in this suit, for the property in suit was purchased by the widow out of self acquired property of her husband); that she enjoys the right of adoption without the permission of her husband or the consent of his heirs; that a daughter's son may be adopted, and on adoption takes the place of a begotten son. It also appears proved by the more reliable evidence that on adoption the estate taken by the widow passes to the son as proprietor."

In a later case in Madras, *Sukhdevdas Ramprosud v. Choti Bai and Others*, the officiating Chief Justice held:—

"I am however, inclined to think that although the widow held an absolute estate from her husband, the adoption of defendant would have the effect of vesting that estate in him."

9. Question (iii): *Ante-adoption agreement dated 25th August 1896*
—*Not void or voidable etc.* :

Whether an agreement of the nature as we are considering is binding on the adopted son admits of grave doubts. The natural father and the adoptive mother entered into an agreement, and agreed to certain conditions which have been reproduced above in the statement of facts. The natural father, however, could not curtail the rights of the minor in the way he has done. Paragraph 15 of the agreement is as follows:—

"The said Sohanmul Chordia shall by virtue of his adoption acquire no present interest whatever in the estate left by late Sha Manmul or in the business of Sha Agarchand Manmul and the same shall be considered the property of the said Sada Kuvar subject to the dispositions hereby provided."

This is an agreement definitely against the interest of the minor and is not of the class of cases that holds that reasonable covenant in the

agreement reserving a life interest by the widow may be held to be valid. The decision of the Privy Council in 50 Madras 508 (*Krishnamurthy Ayyar v. Krishnamurthy Ayyar*) has a great bearing on this case. At page 527 Viscount Dunedin delivering the judgment of the Board observed as follows:—

“But the consensus of judgments seems to solve these two questions in this way, namely, that the consent of the natural father shows that it is for the advantage of the boy, and that the mere postponement of his interest to the widow's interest, even though it should be one extending to a life interest in the whole property, is not incompatible with his position as a son. Their Lordships are, therefore, prepared to hold that custom sanctions such arrangements.”

“As soon, however, as the arrangements go beyond that, *i.e.*, give the widow property absolutely or give the property to strangers, they think no custom as to this has been proved to exist and that such arrangements are against the radical view of the Hindu Law. Their Lordships are, therefore, against the idea of a general proposition that all arrangements consented to by a natural father, and of benefit to the boy in the sense that half a loaf is better than no bread, he is better with an adoption with truncated rights than with no adoption at all, are valid.”

In the case before us, the effect of the agreement is to do away with the entire rights of the son and such an agreement is not binding. The next question for consideration is whether such an agreement is void or voidable. It is stated in 1940 Edition of Mulla's Hindu Law, at page 554, that an agreement going beyond that sanctioned by custom does not bind the minor, it is not void and it may be ratified by the adopted son. In support of this view the cases reported in *Ramasami v. Venkataramaiyan*¹, *Kali Das v. Bajai Shanker*², and *Subramaniam Chettiar v. Velayudam Chettiar*³ are cited.

10. We have examined these cases and do not find that an agreement of this nature where it absolutely does away with the rights of the minor to succeed can be regarded as reasonable or voidable. Such an agreement is altogether void.—Where an agreement is fair and reasonable it may be ratified but not an agreement of this nature: *Krishnamurthy Ayyar v. Krishnamurthy Ayyar* (50 Madras 508).

11. Question (iv): *Being absolute owner—whether there is right to give the property as gift to daughter-in-law.*

Being an absolute owner of the property, Sada Kuvar, it is contended, had every right to give it as a gift to her daughter-in-law, Udai Kuvar, in 1918. This point is also covered by the decision on the

(1) (1879) Mad. 91.

(2) (1891) 13 All. 391.

(3) (1932) 55 Mad. 408.

previous point that she is not the absolute owner after the adoption and she had no right to give anything to the daughter-in-law in that year. Further, the daughter-in-law herself had by her own right as the widow of Sohanmul, become entitled to this property.

12. Question (v):—*Gift of rupees four lakhs to two grandsons and daughter-in-law by Udai Kuvar.*

According to the discussions above and from the pedigree, Udai Kuvar became entitled to the whole property absolutely being the sonless widow of her husband, Sohanmul. Before any adoption, she could make gifts or alienations but not after adoption. When Mohanmul was adopted it will follow from the previous decisions and authorities cited that he became the owner of this property and divested Udai Kuvar.

13. Question (vi): We find that Sohanmul, during his lifetime, and Mohanmul, from the date of adoption, up to the date of his mother's death in April 1931, accepted the position that Sada Kuvar and Udai Kuvar were each in their turn the absolute owners of the property and acted accordingly.

14. Question (vii): The contention is that this position has been accepted by the Department as well as the parties themselves. It was now not competent for the Income-tax Officer to go back on this accepted position and dispute the ownership of the properties and say that a particular person was not the owner and that another particular person should be deemed to be the owner and that a person had no right to act as he or she did. These are vital points for the determination of this appeal.

15. From the discussion of the case law as above we may have come to the conclusion that the property is the joint family property and that all the members of the family pedigree mentioned above became jointly entitled to the properties in their possession. The Department, however, on the basis of the returns made by Sada Kuvar and Udai Kuvar respectively accepted them individually as owners of the property in the years of assessment in which they were in possession. The present Income-tax Officer went into the matter and has given a finding which appears to be correct according to law, namely that the property can be said to be a joint family property and that the assessment should be made in the status of a Hindu undivided family and not that of an individual as claimed by the respondent to this appeal.

16. It has been held on several occasions that the assessment of each year is an independent assessment and the rules of *res judicata* and *estoppel* do not apply to the income-tax proceedings. The correct state of affairs has to be ascertained and the assessment made accordingly. The rights of the Income-tax Officer to make any such assessment

departing from the previous position were considered in the following cases :—

Sankaralinga Nadar Bros. v. Commissioner of Income-tax, Madras [1929] (4 I.T.C. 226).

Messrs. Deokinandan & Sons v. Commissioner of Income-tax, Delhi [1930] (4 I.T.C. 398).

Commissioner of Income-tax, Madras v. Harveys, Ltd. [1940] (8 I.T.R. 307).

17. One other argument was advanced on behalf of the appellant that the person or persons who gave and the person or persons who received the properties were also owners as members of a Joint Hindu family, that the businesses in the names of Mohanmul, and Ratanchand Parasmal, which later were conducted by Parasmal and Ratanchand respectively were conducted from their commencement with the aid of the family funds, and that the parties had only jointly managed the entire business and in fact a specific fund which was earmarked in the name of a specific person, has been administered in the manner in which it was agreed to be dealt with and the matter of gifts, etc., in 1930 was merely sought to be deduced from the entries in the books of account. We must observe that on the basis of the finding that the ante-adoption deed was not valid, this action of the parties would lead to the inference that the properties held were of the Joint Hindu family. Though we agree with the Income-tax Officer that the property may be said to belong to the Hindu undivided family, for the reasons presently stated, we do not agree that the position so far accepted and acted upon should be departed from after a lapse of so many years. The parties have evidently accepted the position of allotment by gifts and there have been separate dealings in regard to such assets as found recorded in the several books of account. This leads to the irresistible inference that they have accepted the ante-adoption agreement and have not chosen to consider it invalid.

18. The decision, moreover, on the question of validity of the ante-adoption agreement, dated the 25th August 1896, and the rights of the parties arising in law are unquestionably beset with difficulties. The Appellate Assistant Commissioner has taken a contrary view of the matter. We feel that though the view of the Income-tax Officer is justified in law in our opinion, yet from the manner in which the parties have themselves chosen to accept their respective rights and positions, it is not possible to say now that the property is a joint family property. The parties have dealt with the property on the basis of the ante-adoption agreement for the last 45 years. The Department also has accepted the position as correct so far. It is true as held above

that the Income-tax Officer can change his view, but it should be for some reason or on any fresh material and not on account of a mere change of opinion after such a long interval on the question of the validity of an action that took place years back. The parties have held the amount given by Sada Kuvar as their own and have, in their books of account, dealt with the amount separately as separate property. To disturb this position acted upon from 1896 after such a long lapse of time will not, we think, be right. The parties themselves have not raised any dispute and have not taken any steps so far against the accepted position in any manner. Nobody has challenged the position so far. The Income-tax Department is an independent third party and although it can go into the question as to what the position of the parties is they cannot allocate the rights of the parties after a lapse of so much time as 45 years, which the parties themselves do not claim. This is not a case in which the real nature of the transactions is to be found after the interval but this is a case in which the assessment is to be arrived at on the basis of the dealing of the parties. We think, therefore, that it would not be right to disturb the position adopted by the Department hitherto and we uphold the Appellate Assistant Commissioner in treating the parties as "Individuals" and not as members of a joint Hindu family, a position accepted for long between the Department and the respondent.

19. The result is that this appeal preferred by the Department is rejected.

20. Before taking leave of this matter we must say that the investigation of the matter by the Income-tax Officer has impressed us for its thoroughness. Although we could not agree with him finally for the reasons stated above, yet we must say that his opinion on the legal points appears to be right. We must also observe that the Appellate Assistant Commissioner too has dealt with the case with marked ability."

STATEMENT OF CASE.

On the application of the Commissioner under Section 66 (1) of the Income-tax Act, 1922, the Appellate Tribunal referred the case to the Madras High Court.

"The Commissioner of Income-tax, Madras, seeks reference to the High Court of Judicature at Madras, on the following question of law as arising out of our order dated the 10th April 1942 in appeal R.A.A. No. 80—Madras of 1941-42:

"Whether in the circumstances of the case the Bench are right in holding that the Income-tax Officer was not entitled to assess the income of the businesses carried on in the names of Ratanchand, Paras-

mal and Naini Kuar (sons and wife of the respondent) as the income of the Hindu undivided family in the hands of the respondent?"

2. The respondent has filed his objection and has contested the position that the question formulated by the applicant arises out of the findings of fact arrived at by this Bench of the Tribunal. It is contended that the question sought to be referred raises in general terms the correctness of the order of the Income-tax Officer making a combined assessment of the income of the business carried on in the names of Ratanchand, Parasmal and Naini Kuar as the assessable income of the respondent.

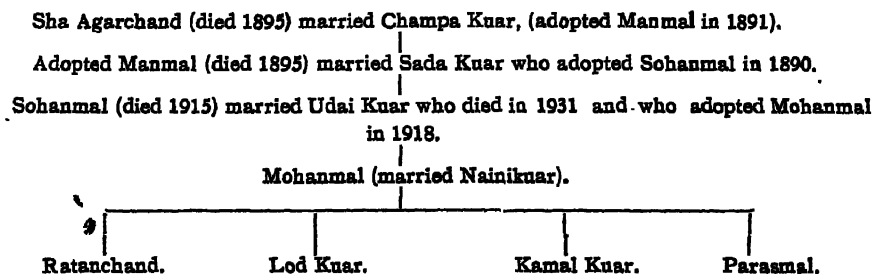
3. We have considered the application and the objections thereto and have heard the learned counsel appearing for both the parties and have come to the conclusion that the question which will be stated hereafter does arise and we, therefore, proceed to state the case for reference to the High Court.

4. For the assessment year 1939-40 Mohanmal Chordia was assessed as a Hindu undivided family on an income which included the income of the businesses conducted in the names of his sons, Ratanchand and Parasmal, and in the name of his wife, Naini Kuar. These businesses were started with the gifts of money made to Ratanchand, Parasmal and Naini Kuar by Udaikuar, the adoptive mother of Mohanmal. The inclusion of these incomes in the assessment made on him is in question.

5. The facts as found or admitted are as follows :—

The respondent belongs to a family of Oswal Jains.

The pedigree of the family is as stated below :—



Sha Agarchand died on 12th February 1891 leaving a 'will' dated the 4th February 1891 bequeathing his properties to Manmal. Manmal was adopted by his widow Champa Kuar on 26th February 1891. He died intestate on 5th June 1895. His widow, Sada Kuar, obtained Letters of Administration to her husband's estate on 12th July 1895. She adopted Sohanmal. There was an ante-adoption agreement dated the 25th August 1896. Sohanmal was adopted by Sada Kuar

on 31st August 1896. Sohanmal also died intestate in July 1915 leaving a widow, Udai Kuar. Sada Kuar gifted the properties to Udai Kuar by means of a gift deed dated the 14th April 1918. Sada Kuar died in 1928. Udai Kuar adopted Mohanmal in May 1918. She died in April 1931. She made gifts to her grandsons and daughter-in-law in October 1930. It is these gifts that form the subject matter of the contest between the parties.

6. The Income-tax Officer held that the income of the businesses standing in the names of Paramsal, Ratanchand and Naini Kuar could be assessed as the income of the Hindu undivided family of the applicant. The Appellate Assistant Commissioner on appeal held that Jains were not governed by the Hindu Law, that on adoption of a son by a widow the estate vested in the widow was not divested and that the gifts by Sada Kuar and Udai Kuar were consequently valid and operative.

7. On a consideration of the facts as also of the law this Bench of the Income-tax Appellate Tribunal came to the following conclusions :—

(a) that the respondent though a Jain was governed by the Hindu Law,

(b) that Sada Kuar when she got her husband's property on his death took it as her absolute property and that when she adopted Sohanmal her estate was divested and vested in the adopted son,

(c) that the ante-adoption agreement of 25th August 1896 taking away the rights of the adopted son in the estate was void,

(d) that after the adoption of Sohanmal, Sada Kuar not being the absolute owner of the property had no right to make a gift of it to Udai Kuar and that after the death of Sohanmal, Udai Kuar herself in her own right as the widow of Sohanmal became entitled to the property,

(e) that on the adoption of Mohanmal he became the owner of the property and divested Udai Kuar of the estate that was vested in her before his adoption,

(f) that Sohanmal during his lifetime and Mohanmal from the date of the adoption to the date of Udai Kuar's death in April 1931 accepted the position that Sada Kuar and Udai Kuar were each in their turn the absolute owners of the property and acted accordingly,

(g) that though it may be said that the properties belonged to a Hindu undivided family yet inasmuch as the parties have themselves accepted their rights on the basis of the gifts, it is not possible to say now that the property is the joint family property, and

(h) that the Income-tax Department cannot claim or allocate the rights of parties after a lapse of 45 years in a manner which the parties themselves do not claim.

On these findings we held that the income of the businesses in the names of Ratanchand, Parasmal and Naini Kuar could not be assessed as the income of a Hindu undivided family. The Department has now applied for a reference under Section 66 (1) of the Income-tax Act and we, accordingly, refer the following question for the decision of the High Court :

Question of Law Referred :

“ Whether in the circumstances of the case the income of the businesses in the names of Ratanchand, Parasmal and Naini Kuar, sons and wife of the respondent is assessable as the income of a Hindu undivided family in the hands of the respondent ? ”

8. The papers mentioned in the index annexed will form the paper book in this case. ”

K. V. Sessa Ayyangar, for the Commissioner.

P. B. Srinivasan, for the Assessee.

JUDGMENT.

(Judgment of the Court was delivered by the Hon'ble the Chief Justice).

The Income-tax Appellate Tribunal, Calcutta Bench, has at the instance of the Commissioner of Income-tax, Madras, made this reference. It concerns the assessment of four money-lending businesses. The Commissioner of Income-tax says that these businesses are really the businesses of a joint Hindu family and the profits should be assessed on that basis. The Tribunal has held that they are separate businesses and the profits should be assessed separately. The first and most important business is carried on in the name of Sha Agarchand Manmul and the three other businesses under the styles of M. Ratanchand, M. Parasmal and Bai Naini Kuar respectively. The question which has been referred reads as follows :—

“ Whether in the circumstances of the case the income of the businesses in the names of Ratanchand, Parasmal and Naini Kuar, sons and wife of the respondent is assessable as the income of a Hindu undivided family in the hands of the respondent ? ”

In order to understand the position it is necessary to go back to the year 1891. On the 12th February of that year Sha Agarchand, an Oswal Jain, the founder of the business now carried on under the style of Sha Agarchand Manmull died, leaving a widow Champ Kuar, but no issue. On the 26th February 1891 Champ Kuar adopted a son, Manmull, who married Sada Kuar. On the 5th June 1895 Manmull died without issue, but he was survived by his widow. In the month of August 1896 Sada Kuar contemplated adopting one Sohanmull and on

the 25th of that month she entered into an agreement with the father of Sohanmull under which she was to make the adoption, but it was not to operate to divest her of the estate which had devolved upon her on her husband's death. On the 31st August 1896 Sada Kuar adopted Sohanmull. He died in the month of July, 1915. On the 14th April 1918 Sada Kuar, gave the business and its assets to her daughter-in-law Udai Kuar. In the month of May 1918 Udai Kuar adopted Mohanmull, the assessee in this case. Mohanmull married Naini Kuar and by her has two sons (Ratanchand and Parasmal) and two daughters (Lod Kuar and Kamal Kuar). Sada Kuar died in 1923. In October 1930 Udai Kuar gave to each of her grandsons Rs. 1,50,000/ and to their mother, Naini Kuar, Rs. 1,00,000/- Udai Kuar died in 1931. Mohanmull, his wife and children are still alive. With the moneys given to them by their grandmother the businesses now carried on under the style of M. Ratanchand, and M. Parasmal, respectively were started and with the Rs. 1,00,000 which Naini Kuar received the business now standing in her name was launched. Mohanmull succeeded to the main business of Sha Agarchand Manmull on the death of Udai Kuar in 1931.

From 1931 until the assessment year 1939-40 the four businesses were assessed separately to income-tax. In that year the Income-tax Officer held that the four businesses were really one and carried on by the joint family of which Mohanmull was the head. The Income-tax Officer formed the conclusion that with a view to the evasion of taxation at the appropriate rate Mohanmull had started three subsidiary businesses and had kept separate sets of books in respect of each of them though they were in reality parts of the main business. This finding was reversed on appeal by the Appellate Assistant Commissioner.

The appellate Assistant Commissioner was of the opinion that it was not a matter of attempting to evade payment of tax at the appropriate rate. The businesses were separate and they had been rightly assessed separately from 1931 onwards. The Commissioner of Income-tax appealed to the Income-tax Appellate Tribunal which agreed with the Appellate Assistant Commissioner. The findings of the Tribunal are summarised in paragraph 7 of the statement of the case as follows:—

- (a) The respondent though a Jain was governed by the Hindu Law.
- (b) Sada Kuar when she got her husband's property on his death took it as her absolute property and when she adopted Sohanmull her estate was divested and vested in the adopted son.
- (c) The ante-adoption agreement of 25th August 1896 taking away the rights of the adopted son in the estate was void.
- (d) After the adoption of Sohanmull Sada Kuar not being the absolute owner of the property had no right to make a gift of it to

Udai Kuar and after the death of Sohanmal, Udai Kuar herself in her own right as the widow of Sohanmal became entitled to the property.

(e) On the adoption of Mohanmal he became the owner of the property and divested Udai Kuar of the estate that was vested in her before his adoption.

(f) Sohanmal during his life time and Mohanmal from the date of the adoption to the date of Udai Kuar's death in April 1981 accepted the position that Sada Kuar and Udai Kuar were each in their turn the absolute owners of the property and acted accordingly.

(g) Though it may be said that the properties belonged to a Hindu undivided family yet inasmuch as the parties have themselves accepted their rights on the basis of the gifts, it is not possible to say now that the property is the joint family property.

(h) The Income-tax Department cannot claim or allocate the rights of parties after a lapse of 45 years in a manner which the parties themselves do not claim.

It is unnecessary to inquire whether the law which applies to this community of Jains is as stated by the Tribunal. What the Court is concerned with is whether the gifts made by Sada Kuar and Udai Kuar were *bona fide* transactions and were accepted by the members of the family. The finding of the Tribunal is that they were *bona fide* transactions and that they have been accepted as being valid by the family. It follows from what the Tribunal has said in its order on the appeal from the Appellate Assistant Commissioner that the businesses carried on in the names of the two grandsons and the daughter-in-law of Udai Kuar are genuine businesses and are not parts of the business carried on by Mohanmal.

It was open to the members of the family to accept the gifts made by Sada Kuar and Udai Kuar as being valid and binding on them. Mohanmal, the person most concerned does not challenge the validity of the gifts and it is not open to a third party to do so. If the three minor businesses were in fact parts of the main business and had been merely started with a view to evade taxation, the position would have been different, but that is not the position as found by the Tribunal, which is the final arbiter on questions of fact. The Tribunal found that the action of the Department up to the year 1938-39 was on the facts correct and therefore decided the appeal against the Commissioner. In these circumstances the question referred must be answered in the negative.

The respondent is entitled to his costs which we fix at Rs. 250.

Reference answered in the negative.

[IN THE LAHORE HIGH COURT.]
GOVERNOR-GENERAL IN COUNCIL

v.

SARGODHA TRADING COMPANY LTD.

HARRIES, C.J., ABDUL RASHID and BRACKETT, JJ.

March 28, 1948.

INCOME-TAX—COMPANY—WINDING UP—PROOF OF INCOME-TAX DEBT—ASSESSMENT ORDER—EVIDENTIARY VALUE—WHETHER LIQUIDATION COURT ENTITLED TO GO BEHIND ASSESSMENT—BEST JUDGMENT ASSESSMENT AFTER WINDING UP—PRIORITY OF DEBT—INDIAN COMPANIES ACT (VII OF 1918), SECS. 171, 228, 229, 238—INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 23 (4), 27.

In the winding up of an insolvent company the Liquidation Court can go behind an income-tax assessment if there are suspicious circumstances. An assessment order is prima facie proof of the taxable income and the onus of proving that the assessment does not represent the real taxable income rests on the Liquidator.

A company which was in financial difficulties did not file a return of its income on the due date but it was granted an adjournment. Subsequently an order was made for winding up the company and a provisional Liquidator was appointed. After the winding up a return of income not supported by the necessary documents and accounts was made by the manager. The Income-tax authorities gave the company an opportunity to produce the accounts and documents and on its failure to do so, assessed it under Section 23 (4) of the Income-tax Act. The provisional Liquidator who was unaware of these proceedings subsequently applied for an adjournment to file the necessary documents but the Income-tax authorities refused it. They also refused his application under Section 27 of the Income-tax Act for cancellation of the assessment.

Held, that, under the circumstances, the Liquidation Court should treat the assessment as prima facie evidence of the amount of tax due from the company but should permit the liquidator to rebut it, if he could, by producing documents or such other evidence as might be in his possession.

Where a tax did not become due and payable until after the winding up order had been made, the Crown could not claim any priority for the amount of the tax.

It would not be in accordance with justice, equity and good conscience to apply the rule enunciated in IN RE CALVERT [1899] (2 Q.B.D. 145) to India.

Diamond General Insurance Co., In re (C. O. No. 222 of 1937) overruled; Dinshaw & Co. v. Income-tax Officer, Lucknow [1941] (9)

I.T.R. 215; 16 Luck. 599) not followed; *Ex Parte Lennox* [1885] (16 Q.B.D. 815) followed.

Cases referred to :—

Bank of Bihar Ltd. v. Secretary of State (1932) A.I.R. 1932 Pat. 1.

Calvert *In re* (1899) 2 Q.B.D. 145.

Diamond General Insurance Co., *In re* (C. O. No. 222 of 1937).

Dinshaw & Co. v. Income-tax Officer, Lucknow (1941) 9 I.T.R. 215; I.L.R. 16 Luck. 599.

Income-tax Officer, Lucknow v. Lucknow Sugar Works Ltd. (1935) 8 I.T.R. 322.

Kibble *Ex parte* (1875) 10 Ch. A. 378.

Lennox *Ex parte* (1885) 16 Q.B.D. 815.

Tollemache *In re* (1884) 18 Q.B.D. 720.

In the matter of Sargodha Trading Company Limited (In liquidation) and of the claim of Income Tax Officer, Sargodha, and petition under Sections 171, 232 and 228 of the Indian Companies Act for restraining the Income Tax Officer and the Collector, Sargodha, from taking any proceedings against the company in liquidation through the Official Liquidator.

Letters Patent Appeal under Clause 10 of the Letters Patent against the judgment of Mr. Justice Monroe, dated the 8th November, 1940, passed in Civil Original No. 195 of 1939, rejecting the claim.

This case came up for hearing before a Division Bench consisting of Mr. Justice Dalip Singh and Mr. Justice Beckett, and the learned Judges by their order dated the 9th December, 1942, referred it to a Full Bench.

Raj Kishan, for the Income Tax Authorities (Appellant).

Bashir Ahmad, for the Official Liquidator (Respondent).

ORDER OF REFERENCE.

DALIP SINGH and BROCKETT, JJ.—This case raises an important question of law. Even if we differed from the Division Bench it is not the practice of this Court to differ from a Division Bench unless it is clearly wrong and the case would have to go to a Full Bench. As there is a conflict of authority we consider the point should be finally decided by a larger Bench. In the meantime we have suggested to counsel on both sides that this hardly seems the case where a decision should be sought on technical grounds as the facts should now be capable of ascertainment beyond doubt as the books of the Company can be seen by the Official Liquidator and by the Income-tax Authorities. Counsel are willing to see if the matter can be adjusted and for this would ask for time. Hence we refer this case to a larger Bench for decision subject to the orders of the Hon'ble Chief Justice.

Raj Kishan, for the Income Tax Authorities (Appellant.)

Bashir Ahmad and *Amar Nath Kirpal*, for the Official Liquidator
(Respondent.)

JUDGMENT.

HARRIES, C. J.—This is an appeal from an order of the learned Liquidation Judge, dated the 8th of November 1940, rejecting a proof of the Commissioner of Income Tax in liquidation proceedings. The appeal was first heard by a Division Bench but as important and difficult questions of law were involved, the case was referred to a larger Bench. The case has therefore been heard by this Special Bench.

The facts giving rise to this litigation can be shortly stated as follows:—

The Sargodha Trading Company, Limited, now in liquidation, were by law bound to make a return of the income earned by them for the assessment year 1938-39 on or before the 15th of June 1938. The company filed no return and on the 3rd of July 1938 the Commissioner of Income-tax, Punjab, served a notice on the company under Section 22 (4), Indian Income-tax Act, calling upon the company to produce their accounts on the 7th of July 1938. On this date the Manager of the Company appeared before the Income-tax Officer and applied for an adjournment and the 14th of July 1938 was fixed for production of the accounts. On the 12th of July 1938 an order was made to wind up the company and a provisional Liquidator was appointed.

On the 14th of July 1938 the Manager filed a return showing that the company had incurred a loss of Rs. 22,052/- for 1937-38 which was the accounting year for the assessment year 1938-39. This return was not accompanied by a balance-sheet or a copy of the profit and loss account and it is conceded that this was not a return of income contemplated by law. The Manager of the Company was called upon to file copies of the profit and loss account and the balance-sheet by the 28th of July 1938 and he was warned that if such were not filed, an assessment by the tax authorities would be made under Section 23 (4), Indian Income-tax Act.

On the 28th of July 1938 no one appeared on behalf of the company and on the 29th of July 1938 the Income-tax authorities made an assessment under Section 23 (4) of the Act. The income-tax payable as a result of this assessment was Rs. 3,814/3/-.

As I have stated earlier, this company went into liquidation on the 12th of July 1938 and it would appear that the provisional Liquidator was unaware for some time of these proceedings between the Income-tax authorities and the Manager of the Company. On the 5th of August 1938, however, the provisional Liquidator, who had by that time

become aware of the proceedings, applied to the Income-tax authorities for a further adjournment to file the necessary documents but this application was refused and the provisional Liquidator was informed that an assessment had already been made.

On the 13th of August 1938 a notice was served on the provisional Liquidator demanding Rs. 3,814/3/, as tax due from the company. On the 3rd of September 1938 the provisional Liquidator applied for an inspection of the assessment records and this was allowed. On the same date the provisional Liquidator filed an application under Section 27, Indian Income-tax Act, praying that the assessment which had been made under Section 23 (4) should be set aside or cancelled. In this application it was stated that while these proceedings were going on, the company had gone into liquidation; but the application was rejected by the Income-tax Officer. It is to be observed that the liquidator did not pursue the matter further and did not appeal from the decision of the Income-tax Officer, neither did he apply for any review of the order. Later some attempt was made to challenge this assessment but with no result.

On the 23rd of March 1939 the Income-tax Officer called upon the Collector to recover the amount of the tax and on the 20th of June 1939 the Liquidator applied to the liquidation Judge under Sections 171, 228 and 233, Indian Companies Act, to restrain the Collector and the Income-tax Officer from effecting recovery of the tax and to direct them to put in a formal claim for the amount of tax.

An *ad interim* order to stay the recovery of this tax was made and on the 1st of November 1939 this interim order was made permanent. At this hearing counsel for the Income-tax Officials handed in a formal proof of their claim to the Official Liquidator without prejudice to their rights to contest the power of the Official Liquidator to call upon them for any further proof.

The matter again came before the learned Liquidation Judge on the 8th of November 1940 when counsel for the Commissioner of Income-tax said that he was not prepared to prove his claim except by production of the assessment. The learned Judge, following a Division Bench decision of this Court, held that mere production of the assessment was not sufficient and as the Commissioner of Income-tax was not prepared to prove his claim, the claim was rejected.

From this decision the present appeal has been preferred.

The only question which has to be decided in this appeal is whether the liquidator can call upon the Income-tax authorities to prove their debt. According to the Income-tax authorities, production of the assessment is sufficient whereas the liquidator contends that the

Court is entitled to go behind the assessment and to call for proof that the amount of tax to which the Company was assessed was actually due.

It is clear in this case that the Crown has no priority for the amount of the tax in question. The tax did not become due and payable until after the winding up order had been made and therefore it is not a debt for which priority can be claimed, see Section 230, sub-sections (1) and (5), Indian Companies Act, and *The Bank of Bihar, Ltd. v. Secretary of State*¹. In fact this point as to there being no priority is conceded by Counsel for the Commissioner of Income-Tax.

By Section 229, Indian Companies Act, it is provided that in the winding up of an insolvent company the same rules shall prevail and be observed with regard to the respective rights of secured and unsecured creditors and the debts provable as are in force for the time being under the law of insolvency with respect to the estates of persons adjudged insolvent; and all persons who in any such case would be entitled to prove for and receive dividends out of the assets of the company may come in under the winding up, and make such claims against the company as they respectively are entitled to by virtue of this section.

The rules governing proof of debts in insolvency are set out in Section 34, Provincial Insolvency Act. That section provides:—

“(1) Debts which have been excluded from the schedule on the ground that their value is incapable of being fairly estimated and demands in the nature of unliquidated damages arising otherwise than by reason of a contract or a breach of trust shall not be provable under this Act.

(2) Save as provided by sub-section (1) all debts and liabilities, present or future, certain or contingent to which the debtor is subject when he is adjudged as insolvent, or to which he may become subject before his discharge by reason of any obligation incurred before the date of such adjudication, shall be deemed to be debts provable under this Act.”

It is observed that there are similar sections in the English Bankruptcy Act.

It is common ground between the parties that an Insolvency Court can go behind a decree—or a judgment, as it is called in England—and call upon the decree-holder to prove his debt. Mere production of the decree will not suffice and evidence that the decree is based upon a legal debt will be demanded in all cases where there are circumstances giving rise to suspicion. It is, however, contended by the present appellant that an assessment does not stand on the same footing as a decree or judgment. Whilst conceding that an Insolvency

(1) (1932) A.I.R. 1932 Pat. 1.

Court, and therefore a Liquidation Court, can go behind a decree, it is urged that it cannot go behind an assessment. To support this argument reliance is placed upon an English case *In re Calvert*¹, which was followed in India in *Messrs. Dinshaw & Co. v. The Income-tax Officer, Lucknow*².

In the case of *In re Calvert* referred to above, Wright, J., held that "the rule that on proof for a judgment debt the Court will go behind the judgment and ascertain whether there is a provable debt, does not apply to a proof for assessed taxes". Where therefore a debtor, who had carried in a scheme of arrangement, applied to expunge a proof for an assessment to Income-tax under Schedule D (which had not been appealed against), on the ground that he had made no profits assessable to duty, the application was dismissed but without prejudice to any application he might be advised to make to the Inland Revenue under the Board of Trade Regulations of May 1888. Wright, J., in his judgment states that in the case of judgments or decrees there is always a danger that the insolvent has colluded with the decree-holders. A person about to become insolvent might submit to a number of fictitious claims and permit his friends and relations to obtain collusive decrees against him and later the insolvent by means of these decrees might obtain a share of the assets which he would not otherwise be entitled to. According to Wright, J., it is because of this fear of collusion that an Insolvency Court or a Liquidation Court will investigate the decrees and examine the debts on which they are founded. Wright, J., then points out that there is no fear of such collusion between a person in financial difficulties and the Income-tax authorities. In his view it would be inconceivable that a person about to become insolvent would ever collude with tax authorities presumably because the latter would never allow the insolvent a share in any dividend paid to them. As there was no fear of collusion, Wright, J., held that there was no reason in the case of assessments why the Court should go behind the actual assessments and ascertain whether any income had been earned, upon which the assessments were founded. The learned Judge also pointed out that in the case of assessments there was no question of consideration as in the case of a judgment and therefore the Insolvency or Liquidation Court could not in the case of assessment go into the question of consideration as it could do in a judgment.

It is to be observed that the insolvent in the case of *In re Calvert*¹ had another remedy under the Board of Trade Regulations issued under the Bankruptcy Act, 1883, dated May 1888. By those Regulations it

(1) (1899) 2 Q.B.D. 145.

(2) (1941) 9 I.T.R. 215; I.L.R. 16 Luck 599.

was provided that "where income-tax is outstanding under Schedule D the Inland Revenue authorities will, on receipt of an affidavit by the debtor, with a certificate by the Official Receiver or trustees setting out that the debtor has made no income taxable under such schedule forego all claim to payment of the tax, whether the same is payable in full under Section 40 of the Bankruptcy Act, 1883, or otherwise." It is to be observed, however, that there is no such alternative remedy in India. If the Insolvency Court or the Liquidation Court is not entitled to go behind the assessment, the assessment cannot be challenged in any other way.

In *Messrs. Dinshaw and Co. v. Income-tax Officer, Lucknow*¹ a Bench of the Oudh Chief Court followed the case of *In re Calvert*² and overruled an earlier single Bench decision of the same Court, *Income-tax Officer, Lucknow v. Lucknow Sugar Works Ltd.*³ in which it had been held that an Insolvency or Liquidation Court could go behind an assessment.

Even if the case of *In re Calvert*² correctly states the law in England, I would hesitate to apply the same rule in India. In this province in particular a very large number of companies have been formed in recent years and experience has shown that directors and responsible officers of these companies have not fully realised their duties and obligations. At present there is a real danger, when a company is in financial difficulties, that demands for returns of income may be completely ignored with the result that assessments under Section 23 (4), Indian Income-tax Act, might well be made when no income had been earned. Balance sheets are, often negligently and sometimes fraudulently prepared and cases have occurred in this Court when for fraudulent purposes purely imaginary profits have been shown as having been earned and income-tax paid upon such profits. Such cases are referred to in the judgment in the case of *In re Diamond General Insurance Company*⁴, to which reference will be made later in this judgment. To apply the rule as laid down in the case of *In re Calvert*² to this province would in many cases seriously prejudice the rights of other creditors and confer an unfair advantage upon the Income-tax authorities. Further, as I have stated, the insolvent or the liquidator of a company in liquidation has no alternative remedy in India as in England because in this country there is no provision corresponding to the Board of Trade Regulations of May 1888 to which reference has already been made. In my judgment it would not be in accordance with justice, equity and good conscience

(1) (1941) 9 I.T.R. 215; I.L.R. 16 Luck. 599. (3) (1935) 3 I.T.R. 322; 1935 O.W.N. 791.

(2) (1899) 2 Q.B.D. 145.

(4) C.O. No. 222 of 1937.

to apply the rule enunciated in *In re Calvert*¹ to India even if that case be regarded as correctly decided in accordance with English Law.

In my view, however, the rule enunciated by Wright, J., in *In re Calvert*¹ is not in accordance with other English authorities which are to be preferred to the case of *In re Calvert*¹.

The leading case is that of *Ex parte Kibble*². In that case an infant, before the passing of the Act gave a bill of exchange, payable after his majority, to a jeweller in payment for jewellery. After his majority, and after the Act came into operation, the creditor obtained judgment by default against the infant in an action on the bill of exchange, and then took out a debtor's summons and, on his failing to comply with it, filed a petition for adjudication of the debtor. The second section of the Infant's Relief Act provided that no action could be brought on any ratification made after full age of a contract made during infancy. The Court of Appeal in England held that the Court of Bankruptcy would look into the consideration for the judgment and that if the conduct of the debtor, in allowing the judgment to go by default against him, operated as a ratification of the bill of exchange, such ratification was rendered void by the second section of the Act and the petition for adjudication was consequently dismissed.

It should be observed that *Ex parte Kibble*² is not a case of collusion between the debtor and the decree-holder but is a case where the debtor merely allowed the decree to be passed in default. Yet the Court had no hesitation in examining the debt upon which the decree was founded and in holding that there was no legal debt to support bankruptcy proceedings. At page 378 Mellish, L.J., observed :—

"It is quite clear that in the Court of Bankruptcy the consideration for a judgment may be investigated, particularly when the judgment has gone by default. I do not mean to say that this rule applies to such an extent that in every case in which a defendant has a good defence to an action and does not plead it, as, for instance, where he had no notice of dishonour of a bill of exchange, the Court of Bankruptcy would allow the creditors to go behind the judgment. The real question must always be whether there was a good consideration for the debt, and we have therefore to consider whether there was a good consideration in this case".

The case of *Ex parte Kibble*² was followed by the Court of Appeal in England in the case of *In re Tollemache*³. That was a case where collusion was suspected and the Insolvency Court felt bound to investigate whether the decree was passed upon a good and valid debt. At page 725, Cotton, L.J., observed :—

(1) (1819) 2 Q.B.D. 145.

(2) (1875) 10 Ch. A. 373.

(3) (1884) 13 Q.B.D. 720.

"The proof is founded simply on the judgment, for there is no evidence of any indebtedness by the bankrupt independently of the judgment. What is the law on the point? In bankruptcy a judgment certainly stands in a different position from that in which it previously stood as against the debtor himself, because the rights of the other creditors of the bankrupt have supervened. When a person is *sui juris* a judgment against him is very strong *prima facie* evidence against him of the existence of a debt; if he disputes it, he must satisfy the Court that there is some reason which requires that the judgment should be set aside. It has been contended that in bankruptcy a judgment ought to be entirely disregarded, but it is unnecessary to decide that point now. I will deal with the case on the footing that the judgment cannot be disregarded, but that there may be other facts which entitle the Court to go behind it."

In a subsequent case, *Ex parte Lennox*¹, the Court of Appeal in England following the earlier cases to which I have made reference, held that the Court of Bankruptcy had power to go behind a judgment and inquire into the consideration for the judgment debt, not only at the instance of the trustee in the bankruptcy of the debtor upon the question of the proof of the debt, but also at the instance of the judgment debtor himself upon the hearing of a petition by the judgment creditor for a receiving order, even though the debtor has consented to the judgment; and, if on the hearing of the petition facts are alleged by the debtor, of which evidence is tendered, and which, if proved, would shew that, notwithstanding the judgment, there is, by reason of fraud or otherwise, no real debt, the Court ought not to make a receiving order without first inquiring into the truth of the debtor's allegations. At page 325 Cotton, L.J., observed:—

"It has been long established, as regards the proof of a debt in bankruptcy that the trustee, acting on behalf of the creditors, can go behind a judgment, and that, although the judgment is *prima facie* evidence of a debt due to the creditor who claims to prove for the judgment debt, yet the trustee, on behalf of the creditors, may shew that in fact the judgment does not establish a debt. That rule is founded upon this principle that, under whatever circumstances a judgment may have been obtained against the bankrupt, yet no act of his—collusion, compromise improperly entered into, or anything else—ought to prejudice the rights of the other creditors, because the assets ought to be distributed in the bankruptcy only amongst the honest *bona fide* creditors of the bankrupt."

(1) (1885) 16 Q.B.D. 315.

At page 329 Lindley, L. J., referring to an observation of Mellish, L. J., in *Ex parte Kibble*¹, remarked:—

“What does that mean? It means, I think, that although the judgment debtor could not go behind the judgment, the Court of Bankruptcy will not allow itself to be put in motion at the instance of a person who is not a real creditor. The Court will not allow bankruptcy proceedings to be had recourse to for the purpose of enforcing debts which are fictitious, and not real, even although they are in the form of judgment debts.”

The effect of these cases appears to be that the Insolvency Court will always go behind a judgment or decree if there exist reasons to believe that the debt is fictitious and not a real legal debt. The Court of Bankruptcy has to safeguard the interests of the debtor and of all the creditors and no act of the debtor ought to prejudice the rights of the other creditors. If the insolvent has colluded with a creditor, such (*sic*) will not prejudice the other creditors. And similarly if the insolvent by his inability or carelessness has failed to contest an unfounded claim, such also will not prejudice the creditors and the Court will in proper cases examine the alleged debt to see whether it in fact exists.

An assessment made by the Income-tax authorities is a determination by a special procedure of the income of an individual or company, usually based upon an examination of the accounts. Where no accounts are submitted and no return of income filed, the assessment is made under Section 23 (4), Income Tax Act, and is made on the basis of such materials as are available. However it is made, it is a determination made according to law of the taxable income of the assessee. If an examination shows there is no income, then there can be no assessment and in many ways an assessment is similar to a decree or judgment. It is a determination of the assessee's income upon which tax is payable just as a judgment is a determination of the debt due and owing from one party to another. If there is reason to believe that an assessment has been based on non-existent or fictitious profits or gains, I cannot see why an Insolvency Court or Liquidation Court should not go behind such an assessment as it can in the case of a judgment or decree. The tax payable after such assessment is a debt due to the Crown and if there is in fact no income and therefore no debt, there appears to be no reason why the Crown should be in a better position than any other creditor. If a court in a proper case can examine the alleged debt on which a decree is founded, why cannot it examine the alleged income, profits or gains on which an assessment and the tax due are based? Wright, J., in *In re Calvert*² points out that there is no

(1) (1870) 18 Ch. A. 373.

(2) (1899) 2 Q.B.D. 145.

consideration for an assessment as there is for a judgment or a decree but with respect this is really a matter of language. The position is very similar where there is no debt to support a decree and where there is no income, profits or gains in fact to support an assessment and the amount of tax demanded.

In my view it is clear that the fear of collusion was not the main reason for the rule that insolvency or Liquidation Courts could go behind decrees. The real reason is that insolvency and Liquidation Courts must safeguard all the parties and must not allow any creditor to receive any portion of the assets unless they are satisfied that that creditor has a real debt. I can see no reason why the Income Tax authorities should be entitled in the liquidation of this company to obtain payment of their demand if it can be shown that there was no debt really due to them, in other words, if it can be shown that no income was earned, upon which tax is payable.

In my judgment the true rule is that laid down in *Ex parte Lennox*¹, in which it was laid down that a judgment is *prima facie* evidence of the debt but not conclusive. In cases where the facts give rise to a suspicion that there is no real debt, the Court can go behind the judgment or decree but the onus of showing that the judgment or decree does not represent a real and valid debt, rests on those who seek to challenge it. That rule to my mind applies with equal force to assessments and a Liquidation Court can in proper cases go behind assessments though the latter are *prima facie* evidence that certain income was earned and that the amount of tax is due.

The precise point which arises in this case was considered by a Bench of this Court in the case of *In re Diamond General Insurance Co.*² decided on the 25th of May, 1939, in which it was held that the Income-tax authorities must prove their debt and that mere production of the assessment was not sufficient proof. In the absence of any further proof the claim of the tax authorities was dismissed. The learned Single Judge who decided the case now before us followed this earlier Division Bench decision and rejected the claim of the tax authorities holding that production of the assessment was insufficient. The Division Bench which first heard this appeal doubted the correctness of this judgment.

In my judgment this Division Bench decision goes somewhat too far. The assessment is in my view *prima facie* proof of the taxable income, but the Court can go behind it if there are suspicious circumstances. The onus of proving that the assessment does not represent the real taxable income rests, however, on the liquidator.

(1) (1885) 16 Q.B.D. 316.

(2) C. O. No. 222 of 1927, (unreported).

The question arises therefore whether circumstances exist in this case which would entitle the Court to go behind the assessment. In my view the circumstances give rise to grave suspicion that the assessment made by the tax authorities was wholly unwarranted. The company was obviously in financial difficulties and before the assessment was actually made an order for the winding-up of the company had been made on the ground that it could not pay its debts. This would strongly suggest that in the accounting year in question no actual profits could have been made or income earned. After the winding-up order was made, a return of the income not supported by the necessary accounts was made by the Manager of the company and no opportunity was given to the liquidator to furnish further accounts before assessment. Further, the application by the liquidator under Section 27, Indian Income-tax Act, for cancellation of the assessment and for making of a new one, was dismissed. I am not suggesting that the Income-tax authorities did not act properly and *bona fide* but it does appear to me that there is a real danger in this case that an assessment was made when in fact no income was earned or profits made. The assessment was a "best judgment" assessment and it is doubtful whether the Income-tax authorities had materials before them, upon which a fair assessment could be made. They were, of course, entitled to make an assessment in the circumstances, but the question still arises whether the assessment is such that the tax demanded as a result represents a real debt due to the Crown in respect of income-tax. In my judgment, circumstances do exist in this case which would entitle the Court to go behind the assessment and to disregard it if the materials placed before the Court by the liquidator establish that no income was earned or profits made during the year in question. The onus will rest upon the liquidator and if the latter fails to discharge the onus, the assessment must, of course, stand. In my view the learned Liquidation Judge was not right in rejecting the claim of the Commissioner of Income-tax without investigation. He should have treated the assessment as *prima facie* evidence and permitted the liquidator to rebut it, if he could, by producing documents or such other evidence as might be in his possession.

In the result therefore I would allow this appeal, set aside the order of the learned Liquidation Judge and send the case back to the Liquidation Court to be heard and decided in accordance with the observations which I have made. The costs of this appeal will abide the decision of the Liquidation Judge.

ABDUL RASHID, J.—I agree.

BECKETT, J.—I agree.

Appeal allowed.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS

THE MADRAS AND SOUTHERN MAHARATTA
RAILWAY CO., LTD., MADRAS.

SIR LIONEL LEACH, C. J., and KRISHNASWAMI AYYANGAR, J.

March 3, 1943.

INCOME-TAX—'INCOME'—STATE RAILWAY—GUARANTEED INTEREST PAID BY SECRETARY OF STATE ON CAPITAL CONTRIBUTED BY COMPANY—WHETHER INCOME OF COMPANY—ALTERATION OF CONTRACT—EFFECT—CONSTRUCTION OF AMENDED CONTRACT.

The assets of the Madras and Southern Maharatta Railway Company belonged to the Secretary of State and the Company managed the undertaking under the supervision and control of the Secretary of State. The Secretary of State and the Company contributed to the capital and the former guaranteed interest on the Company's capital at the rate of $3\frac{1}{2}$ per cent. per annum. Under the original agreement between the parties, out of the gross revenue receipts the working expenses and interest on debentures were first to be deducted. The Secretary of State then deducted and retained the guaranteed interest which he had paid to the Company in advance and the balance was thereafter divided between the two parties. It was held that the guaranteed interest received by the Company represented profits made in India. The contract was subsequently amended and under the amended contract the surplus to be divided was arrived at after providing for the payment of certain charges and the guaranteed interest paid to the Company was mentioned as one of these charges :

Held, that the alteration in the contract did not make any difference with regard to the nature of the payment of the guaranteed interest and the amount paid towards such interest was assessable as the income of the Company.

Cases referred to :—

Commissioner of Income-tax, Madras v. Madras and Southern Maharatta Railway Co. Ltd. (1940) I.L.R. 1940 Mad. 889 ; 8 I.T.R. 280.

Madras and Southern Maharatta Railway Co. v. Commissioners of Inland Revenue (1926) 12 Tax Cas. 1111.

Case stated under Section 66 (1) of the Indian Income-tax Act, 1922, by the Income-tax Appellate Tribunal, Calcutta Bench, in Reference 66 R.A. No. 5 (Madras) of 1942-43 : (Referred Case No. 21 of 1942).

STATEMENT OF CASE.

“This is an application asking this Bench of the Tribunal to refer the following questions of law to the High Court of Judicature, Madras. The questions formulated by the applicant are as follows:—

1. Are the profits of the assessee for the purpose of the Indian Income-tax Act exclusive of the amount of the guaranteed interest namely, the sum of Rs. 23,33,333 or in other words is such income only so much of its share apportioned and paid to it by the Secretary of State after ascertaining the surplus divisible between the assessee and the Secretary of State under the terms of the agreement between the parties as modified by the agreement dated 24th March 1937?

2. Is income represented by the guaranteed interest the income of the assessee company and does such income accrue and arise or is it received in British India?

The respondent has submitted a reply submitting that the question is covered by the decision in I.L.R. 1940 Mad. 889 (8 I.T.R. 280) and that he would oppose a reference if the Bench should consider such reference necessary under Section 66 (1) of the Income-tax Act. The respondent however wishes that the question arising in this case is to be stated in the following form:—

“Whether the sum of Rs. 23,33,333 being the equivalent in rupees of the guaranteed interest paid by the Secretary of State for India under the terms of the contracts dated 1st June 1882, 26th June 1908 and 24th March 1937 between the Secretary of State and the Company which was deducted for the purpose of the Company's return for the accounting years 1937-38 and 1938-39 is liable to assessment in the hands of the company?”

The question whether the point in issue is covered by the decision of the Madras High Court is itself a question of law and in our opinion the case is pre-eminently a fit one to be stated to the High Court as it raises a question of law arising from the order passed by this Bench of the Tribunal under Section 33 of the Indian Income-tax Act.

3. *Statement of the case.*—Two appeals R.A.A. Nos. 11 and 12 were disposed of by this Bench of the Tribunal on the 26th February 1942. The facts of the case may be briefly stated:—

The applicant is a company incorporated in England under the English Companies Act. The company received in London a sum of Rs. 23,33,333 as interest on the deposit of the capital of 5 million pounds of the Company invested with the Secretary of State for India in Council at $3\frac{1}{2}$ per cent. per annum. The governing rights of the applicant are mentioned in the agreement of

1882 and the supplemental contract of 1908 to which there have been various amendments from time to time and the one which is alleged to distinguish this case from the previous case of the company was disposed of on similar point by the High Court of Madras and that is on the 24th March 1937. It is contended before us that this modification is another aspect of the matter and makes previous ruling distinguishable in the order passed on the 26th February 1942. This Bench has set out the nature of receipts and has considered the various clauses as urged before us and has come to the conclusion that the amount is not a revenue expense but an income of the company liable to assessment. In this view of the matter the appeal of the applicant was dismissed. The parties are agreed on the facts of the case and the applicant has in paragraph 3 of the application mentioned the finding of fact arrived at by the Tribunal as under :—

“that the nature of the receipt of the sum of Rs. 23,33,333 has to be determined with reference to the terms of the agreement between the assessee and the Secretary of State as modified by the agreement dated 24th March 1937.”

This is actually no finding of fact but is only a statement of agreed facts that the rights are governed by the agreement. The applicant later on in paragraph 4 of his petition which is annexed to this reference urges various arguments. The question will be for the determination of the High Court. On the above statement of the case a question of law that arises will be stated a little later.

4. The second contention urged before us is that the Company is registered in England and receives the sums of money equivalent to Rs. 23,33,333 in England and this sum does not arise or accrue in British India. This point was not taken before the Officers of the Income-tax Department but being a pure question of law we permitted the question to be argued before us and have recorded our finding and have come to the conclusion that the sum accrues to the applicant company in British India and therefore the applicant company is “resident” within the meaning of Section 4-A (c) (b) of the Income-tax Act. This finding, however, is dependent upon the decision of the first question. If the answer be that the assessment was valid and proper the company would be a resident. It is not necessary to refer this as the result would follow from the answer to the first question.

5. We, therefore, refer to the High Court of Judicature at Madras, the following question of law which in our opinion arises from our order above mentioned :—

“Where the sum of Rs. 23,33,333 guaranteed interest on the capital of the applicant company deposited with the Secretary of State for

India received in England was rightly assessed as the income of the applicant ? ”

6. The papers mentioned in the index will form the paper book.

The judgment of the Appellate Tribunal was as follows :—

“ These two appeals Nos. 11 and 12 of 1940-41 are against the assessments for the years 1938-39 and 1939-40 respectively. The questions of law and fact are common and both the appeals will be dealt with by one order.

2. The appellant is a company incorporated in England under the English Companies Act. The main object was the construction and carrying on of a Railway in India. It is controlled by a Board of Directors in London and derives its income from the working of the Railway in India and from investments in England. The rights of the Secretary of State for India and the appellant are governed by a contract entered into in 1882 and by a supplemental contract of 1908. There have been agreed amendments from time to time and the latest is the one of the 24th March 1937 on the basis of which the payment referred to below for the previous years in question had been made.

3. The amount in dispute in either of the appeals is a sum of Rs. 23,33,333 paid by the Secretary of State for India to the appellant during each of the two respective previous years. The sum represents interest at the rate of 3½% on the nominal amount of capital stock of £ 5 millions of the company under clause 15 of the contract of 1908. This amount of the capital, the appellant handed over to the Secretary of State for India for the purpose of its carrying on the business of the Railway.

4. This receipt of Rs. 23,33,333 the appellant claims :

(1) is not its income, and

(2) even if it should be its income, it did not arise or accrue in British India but arose or accrued in London where it was paid to it by the Secretary of State for India. It is further contended

(3) that according to the Article 73 of the Articles of Association of the appellant company this amount as and when received was distributable and had been so distributed amongst the shareholders, and it should therefore, be deemed to be interest paid by the appellant company on the capital borrowed from the shareholders and as such should be allowed as a deduction in computing the income for the purpose of assessment under Section 10 (2) (iii).

4 (a). To appreciate these contentions consideration of some more facts is necessary. The company constructed, equipped and maintained

railways and supplied necessary staff to work the concern. The Secretary of State provided the requisite land in India. The railways including all rails, plants, machinery, rolling stocks etc., are also the properties of the Secretary of State for India. All moneys received by or on behalf of the concern had to be paid to the credit of the Secretary of State in a Government Treasury in India. The appellant had to work under the supervision and control of the Secretary of State who was empowered to appoint one person to be a Director of the Company. The other relevant conditions of the original contract of the appellant with the Secretary of State will be referred to later.

5. The Secretary of State undertook by the contract of 1908 as amended later on the 24th March 1937 to pay to the Company half yearly on the 1st June and 1st December interest at the rate of $3\frac{1}{2}\%$ per annum in respect of the aforesaid sum of £ 5 millions and a further payment of a share of the surplus available from the revenue receipts after adjustments and payment of certain amounts specified in the said amended contract, as detailed later. The method by which the share of the appellant was to be computed according to the amendments to the sub-clauses 3 and 4 of clause 42 of the contract of 1908 in the moneys received was as follows:—

“ The contract of 1882 as amended by any of the existing contracts subsequent thereto shall be construed and have effect as though sub-clauses (3) and (4) of clause 42 were deleted and there were substituted therefor the following :—

[These clauses are quoted in the Judgment of the High Court, *infra* pp. 390-391, and are not therefore printed here—Ed.]

5. Clause 15 of the Contract of 1908 reads as follows :—

“ The Secretary of State will during the continuance of the original contract and the contracts supplemental thereto as hereby varied until the same shall be determined hereunder pay out of the Revenue of India to the Company in London in sterling interest at the rate of $3\frac{1}{2}\%$ per annum for each half year ending on the 30th day of June and the 31st day of December (commencing with the half year ending on the 30th day of June 1908) on the nominal amount of the capital stock for the time being of the Company such interest to be paid on the 1st day of July, or the 1st day of January immediately following the close of such half year.”

6. Prior to the years in question the remuneration to the Company was on the basis of the contract whose terms were below :—

“ Moneys received in each half year which pursuant to this contract are to be treated as received on account of revenue shall be applied as follows (that is to say) :—

(1) Primarily in or towards the discharge of expenditure attributable to the half-year to which the receipts relate.

(2) Secondly in or towards the discharge of expenditure attributable to any previous half-year or half years and not already discharged out of receipts on account of revenue. The further application of receipts provided for by this clause shall be subject to the payment to the South Indian Railway Limited mentioned in Clause Provisional No. 55c (1) hereof, and also to the payment to that Company and to the Kistna District Board respectively, of the rebates referred to in Clause Provisional No. 55c (2) hereof, respectively.

(3) In the next place, in payment of the equivalent in rupees of the interest for the half-year to which the receipts relate, which shall have been paid by the Secretary of State to the Company in respect of the Company's debentures and debenture stock (except the 1,200,000 debenture stock created under the secondly mentioned contract of 31st August 1837) issued with the sanction of the Secretary of State for the purposes of the capital expenditure on the Company's and State lines which shall, for the time being, be outstanding.

The Secretary of State shall be entitled to deduct and retain out of the share of surplus receipts payable to the Company in respect of each year, the equivalent in rupees of the guaranteed interest at $3\frac{1}{2}$ per cent on the Company's capital stock paid by the Secretary of State to the Company.

(4) The surplus (if any) shall, subject to the clause 12 hereof, be divided between the Secretary of State and the Company in proportion to the respective shares in which the capital for the time being of the Company's and State lines (exclusive of debenture capital) shall have been contributed by them.

7. In respect of the assessment for the year 1937-38 this amount of interest at $3\frac{1}{2}$ % on the amount of capital stock of the appellant paid to the appellant was subject matter of a reference to the High Court of Madras, whether it was income assessable to income-tax. In *Commissioner of Income-tax, Madras v. Madras and Southern Maharashtra Railway Company Ltd.*¹, the High Court of Madras held that all the profits of the Company accrued or arose in British India and the amount of guaranteed interest received on the first day of each half year which was claimed by the Company as an allowable deduction, was liable to assessment in the hands of the Company negating its claim.

8. The appellant contends that the subject matter of reference to the High Court in the above case was in nature different from what

(1) (1940) I.L.R. 1940 Mad. 889; 8 I.T.R. 280.

the subject matter of the present appeal is. It is a fresh contract entered into by the Company with the Secretary of State on the 24th March 1937 having effect from the first of January 1938 during the period of the accounting years with which we are concerned. The changes introduced in the agreement have, according to the appellant, rendered nugatory the effect of the decision of the Madras High Court and that of the case reported in 12 Tax Cases, page 1111. It is argued that this payment by the Secretary of State should be deemed to be revenue expenses of the appellant and that the changes in the new agreement bring it into line with the agreement referred to in the case of the *B. N. Railway v. Secretary of State of India*¹.

9. In *Commissioner of Income-tax, Madras v. Madras and Southern Mahratta Railway Company Ltd.*² the learned Chief Justice of the Madras High Court considered the decision in *Bengal Nagpur Railway Company* and observed as follows:—

“This decision, however, conflicts with a later decision in England affecting the Company, the *Madras and Southern Mahratta Railway Company Ltd. v. Commissioners of Inland Revenue*³ and it is this conflict which has given rise to this reference.”

The judgment in the Madras case proceeded further and it was taken for granted in that case that for the purpose of decision of the reference the contract of the Company with the Secretary of State may be taken to be on all fours with the contract of the Bengal Nagpur Railway Co., Ltd., with the Secretary of State. On the authority of the *Madras and Southern Mahratta Railway Company Ltd. v. Commissioners of Inland Revenue*³ it was held that the guaranteed interest paid by the Secretary of State formed part of the company's profits and that recoupment to the Secretary of State out of surplus profits represented distribution of profits. It was further agreed in the Madras Case that the Bengal Nagpur Railway case ought not to be followed.

10. In *Madras and Southern Mahratta Railway Company Ltd. v. Commissioners of Inland Revenue*³ Rowlatt, J., put the question in this way:—

“Are the profits of the Company for the purpose of Corporation Profits Tax the amount of their share before the Secretary of State is recouped, or are they only the balance which is left to them after the Secretary of State is recouped? That is what the question is or, to put it in another way, are they to be taxed on that balance *plus* the amount of the guaranteed interest which is only putting the same in another way.”

(1) (1922) 49 Cal. 815 ; 1 I.T.C. 178.

(3) (1926) 12 Tax Cas. 1111.

(2) (1940) I.L.R. 1940 Mad. 839 ; 8 I.T.R. 280 at p. 293.

11. The contention of the appellant is that the stage at which the appropriation from the earnings of the Railway towards the re-payment to the Secretary of State of the provisional advance payment of the guaranteed interest makes a difference and the fact that it is not from the 'surplus' under the new sub-clause (7) shows that the adjustment by the Secretary of State is not from the profits of the Company. We are unable to accept this contention. At whatever stage the recoupment or adjustment is made of the payment of the 3½% interest on the capital stock of the Company it is ultimately from the earnings of the Railway. As observed by Rowlatt, J., the income of the appellant is the amount of the guaranteed interest paid as well as the share of the surplus of the concern further paid.

12. As regards the argument that the distribution amongst the share-holders of the interest received from the Secretary of State should be treated as interest paid on the borrowed capital, we have only to state that this same argument addressed in the case cited in [1940] [8 I.T.R. 280 did not find favour with the High Court. Paid up capital of a Company is not capital borrowed and what was distributed among the shareholders was dividend.

13. We may in this connection refer to Article 73 of the Company's Articles of Association which reads:—

"Any moneys which may from time to time be paid by the Secretary of State to the Company by way of interest under the provisions of the principal contract or of any modifications thereof, shall be distributed by the Board as dividends among the Members in proportion to the amounts paid up or credited as paid up on their shares by yearly or half yearly payments as the Board may from time to time determine and whether or not such balance of interest or any part of it represents profits of the company or not."

As observed by their Lordships in I.L.R. 1940 Madras:—

"The position is simply that the share-holders have been paid out of the proceeds of the workings of the Railway."

14. The further argument that the amount of the guaranteed payment should not be regarded as profit accruing or arising in British India within the meaning of Section 4 of the Indian Income-tax Act also did not find favour with the learned Judges of the Madras High Court. Matter is concluded by authority binding on us.

15. In respect of every contention raised in this appeal the matter is governed by the ruling reported in 1940 I.T.R. 280 and as such none of them are tenable.

16. *Status of the Company.*—Another objection raised is in regard to the finding that the appellant company is resident and ordinarily

resident in British India. As the "guaranteed interest" paid to the appellant is part of the profits of the company liable to tax, the income arising in British India is greater than the income arising outside British India and the company becomes a "resident" under Section 4-A (c). For the very same reason it also becomes "ordinarily resident" in British India under Section 4-B (c). Its income from investments outside British India is assessable and it is not entitled to the application of the 2nd proviso to Section 4 (1). This point was raised before us although we find that it was not raised before the Appellate Assistant Commissioner or the Income-tax Officer. We find that the status of the Company is "Resident and Ordinarily Resident" in British India.

17. It may also be stated, though it becomes unnecessary to do so, in view of what has been stated above, that under Section 42 of the Income-tax Act as amended in 1939 the income from guaranteed interest and from investments accrued to it from its business connection in British India and becomes assessable to income-tax.

18. The result is that these appeals are dismissed and the orders of assessment are confirmed.

19. A copy of this order will form part of the record in the other appeal No. 12 of 1941 also."

T. R. Venkatarama Sastri instructed by *King and Partridge*, attorneys for the Applicant.

K. V. Sesha Ayyangar, *Advocate*, for the respondent.

JUDGMENT.

(Judgment of the Court was delivered by the Hon'ble the Chief Justice).

This reference raises in a different setting the same question which was decided by this Court in *The Commissioner of Income-tax, Madras v. Madras and Southern Mahratta Railway Company Limited, Madras*¹. Since that case was decided, certain alterations have been made in the contract between the Secretary of State and the company and it is said that the alterations have the effect of relieving the company from the liability to pay income-tax in India on the sum of Rs. 23,38,333/. Admittely the contract was amended with this object in view. If by the amending contract the company can escape this liability it is entitled to make the amendment and the Court has only to decide whether this object has been achieved. The Income-tax Appellate Tribunal, Calcutta Bench, has held that the object has not been achieved, but at the

(1) I.L.R. 1940 Mad. 389; 8 I.T.R. 280.

request of the company it has referred for the decision of this Court the following question:—

“Whether the sum of Rs. 23,33,333 guaranteed interest on the capital of the applicant company deposited with the Secretary of State for India received in England was rightly assessed as the income of the applicant?”

In order to understand the nature of the amendments which have been made in the contract it is necessary to set out certain facts. All the assets of the Madras and Southern Mahratta Railway Company are the property of the Secretary of State. The company manages the undertaking under the supervision and control of the Secretary of State. Both the Secretary of State and the company have contributed to the capital of the undertaking. The Secretary of State's share of the capital is £ 12,750,000/- and the company's share is £ 5,000,000/-. The Secretary of State guaranteed interest on the company's capital at the rate of $3\frac{1}{2}$ per cent. per annum and the figure of Rs. 23,33,333/- represents the sum required to pay this interest. As pointed out in the judgment in the previous case all moneys received by the company in the course of the working of the undertaking are paid over to the Secretary of State. The company is not entitled to use any of the receipts for the purposes of meeting working expenses. These expenses are met from a grant made each year by the Secretary of State.

The contract between the Secretary of State and the company before its recent amendment provided that the moneys received in each half year should be applied in the following order:—(1) In or towards the discharge of expenditure attributable to the half year to which the receipts related; (2) in or towards the discharge of expenditure attributable to any previous half year or half years and not already discharged out of receipts on account of revenue; (3) in payment of interest on debentures; and (4) in payment to the Secretary of State of the amount paid by him to the company in respect of the guaranteed interest on the Company's capital. The surplus was to be divided between the Secretary of State and the Company in proportion to their respective contributions to the capital, exclusive of debenture capital.

In the previous case the question was whether the sum received by the company from the Secretary of State on account of interest on its capital represented profits made in India. The Court held that it did. The payment to the company really meant payment in anticipation of profits and the Secretary of State was to recoup himself out of the profits when they were made.

The contract, as now amended, provides that the receipts shall be

applied :—

“(1) Primarily in or towards the discharge of expenditure attributable to the half year to which the receipts relate.

(2) Secondly in or towards the discharge of expenditure attributable to any previous half year or half years and not already discharged out of receipts on account of revenue. The further application of receipts provided for by this clause shall be subject to the payment to the South Indian Railway Limited mentioned in Clause Provisional No. 55c (1) hereof, and also to the payment to that Company and to the Kistna District Board, respectively, of the rebates referred to in Clause Provisional No. 55c (2) hereof, respectively.

(3) In the next place in repayment in rupees to the Secretary of State of the equivalent of such interest for the half year to which the receipts relate as shall have been paid or shall be payable by the Secretary of State to the company in respect of the Company's debentures and debenture stock which shall have been issued with the sanction of the Secretary of State for the purpose of capital expenditure on the Company's and State lines and which shall for the time being be outstanding.

(4) In the next place in repayment in rupees to the Secretary of State of the equivalent of such interest for the half year to which the receipts relate as shall have been paid by the Secretary of State in respect of interest at the rate of $3\frac{1}{2}\%$ per annum on the nominal amount of the capital stock of the company, under Clause 15 of the Contract of 1908. Provided that if the moneys out of which the repayment mentioned in this sub-clause is to be made are insufficient to make the said repayment the deficiency shall be made good out of the moneys received on account of revenue in the other half of the financial year of which the said half year forms part. Provided also that if the moneys out of which the repayment mentioned in this sub-clause is to be made are in any financial year insufficient to make the repayment of the said amount advanced by the Secretary of State in respect of such financial year the deficiency shall not be made good out of the moneys received on account of revenue in any subsequent year.

(5) In the next place in payment in rupees to the Secretary of State of interest at the rate of $3\frac{1}{2}\%$ per annum or at such other rate as from time to time shall have been agreed upon in the case of further advances made subsequent to the 31st day of December 1937 under the contract of 1908 on the capital advanced by him expressed in rupees for the purpose of capital expenditure on the Company's and State lines which shall consist :—

(a) of the sum of Rs. 16,87,50,000 being the equivalent of £ 12,750,000 (the amount of the capital of the Secretary of State,

mentioned in clause 8 of the contract of 1908 as amended by the contract of 1911 only) less £1,500,000 (the amount repaid to the Secretary of State) converted into rupees at the rate of fifteen rupees to the pound sterling ;

(b) of all advances made by the Secretary of State after the 31st day of December 1907 and before the first day of January 1938 ;

(c) of any further advances which shall be made subsequent to the 31st day of December 1908 ;

Provided always that for the purpose of this sub-clause other than Section (1) thereof any sterling capital which shall have been advanced by the Secretary of State shall be converted into rupees at such rate as was at the date of the advance applicable under the existing contracts for the conversion of sterling payments into rupees.

Provided also that the above mentioned interest shall be calculated for each calendar month on the capital advanced as aforesaid and outstanding at the commencement of each such month and if the amount of such capital outstanding at the end of each month exceeds the amount of such capital outstanding at the commencement of each such month there shall be added to or if the latter amount exceeds the former amount there shall be subtracted from the interest calculated as aforesaid one half of a sum equal to interest on the difference between the said amounts at the rate for the same month.

(6) In the next place in providing for such other debits as it may be agreed should be charged against such receipts.

(7) The surpluses or surplus and deficit for the half years in any financial year shall be combined. The resulting surplus if any shall be divided between the company and the Secretary of State in the following manner that is to say :—

In payment to the Company of one-tenth of the first Rs. 75 lakhs of the said sum.

One twentieth of the next Rs. 15 lakhs.

One-thirtieth of the excess, if any, over the first 90 lakhs.

The balance shall be retained by the Secretary of State."

In our judgment the amendments in the contract do not make any real difference in the position. As before, the company is paid its guaranteed interest by the Secretary of State, who reimburses himself out of moneys received in the course of the working of the railway. The changes introduced by the amendments have no further significance than to alter the stage at which the recoupment is to be shown in the accounts. Originally out of the gross revenue receipts, the working expenses and the interest on debentures were first to be deducted.

Held by the Full Bench (DERBYSHIRE, C.J., MITTER and LODGE, JJ.)—(i) *that, as the dividends of the sterling companies were declared outside British India and paid to the assessee company outside British India, they were income arising to a non-resident outside British India;* (ii) *that Explanation (3) to Section 4 (1) (c) of the Indian Income-tax Act was ultra vires and invalid inasmuch as it was not within the extra-territorial powers conferred on the Indian Legislature by the Government of India Act, 1935;* (iii) *that, as the tax was paid under an illegal demand, it could be recovered back as money had and received;* (iv) *that Section 67 of the Indian Income-tax Act was not a bar to the maintainability of the suit.*

Held further (*Per* DERBYSHIRE, C.J., and MITTER, J.—LODGE, J., dissenting)—*that a suit to recover a sum of money collected as income-tax under an invalid or illegal provision of law was not one concerning 'revenue' in the sense in which that expression is used in Section 226 of the Government of India Act, 1935, and the jurisdiction of the Calcutta High Court to entertain the suit in its Original Side was not barred by that section.*

Per LODGE, J.—*A decision that something is not valid revenue 'concerns the revenue' as much as a decision that it is valid revenue and Section 226 of the Government of India Act was a bar to the suit.*

Cases referred to :

- Alcock, Ashdown & Co. v. Chief Revenue Authority, Bombay (1923) L.R. 50 I.A. 227; 47 Bom. 742; 50 I.A. 227; A.I.R. 1923 P.C. 138; 1 I.T.C. 221.
- Atlee v. Backhouse (8 M. & W. 633).
- Attorney-General for Canada v. Cain and Gilhula (1906) L.R. 1906 A.C. 542.
- Best & Co. v. The Collector of Madras (1918) 35 M.L.J. 23; 1 I.T.C. 18.
- Bhag Chand Dagdusa v. Secretary of State for India in Council (1927) I.L.R. 48 Bom. 87; A.I.R. 1927 P.C. 176; 23 A.L.J. 641; 53 M.L.J. 81; 104 I.C. 257; 54 I.A. 338.
- Bhai Sankar v. The Municipal Commissioners of Bombay (1907) I.L.R. 31 Bom. 604; 9 Bom. L.R. 417.
- Bhimwandiwalla v. Secretary of State for India (1937) A.I.R. 1937 Mad. 536.
- Bradbury v. English Sewing Cotton Co. (1923) L.R. 1923 A.C. 744; 92 L.J.K.B. 736; 129 L.T. 546; 39 T.L.R. 590; 8 Tax Cas. 481.
- Brassard v. Smith (1925) L.R. 1925 A.C. 371.
- Byramjee Jeejeebhoy v. Province of Bombay (1939) I.L.R. 1940 Bom. 58; 7 I.T.R. 670; 3 F.L.J.H.C. 23.
- Central Provinces and Berar Sales of Motor Spirit & Lubricant's Taxation Act, 1938 *In re* (1939) 2 F.L.J. 6; 1939 F.C.R. 18.
- Colonial Bank of Australasia v. Willan (1874) L.R. 5 P.C. 442.
- Colonial Gas Association Ltd. v. Federal Commissioner of Taxation (51 Commonwealth Report 172).
- Colquhoun v. Brooks (1889) 14 App. Cas. 493; 99 L.J.Q.B. 53; 59 L.T. 850; 21 Q.B.D. 52; 61 L.T. 518; 38 W.R. 289; 2 Tax Cas. 490.
- Commissioner of Income-tax, Bombay v. Chunnilal Mehta (1938) L.R. 65 I.A. 332; 6 I.T.R. 521; 1938 Bom. 752; 176 I.C. 15; 42 C.W.N. 1070; A.I.R. 1938 P.C. 232.
- Commissioner of Income-tax, Bombay v. Goldie (1931) I.L.R. 55 Bom. 734; 5 I.T.C. 223.

Commissioner of Income-tax, Bombay Presidency v. Raja Bahadur Bansilal Motilal (1930) I.L.R. 54 Bom. 460 ; 125 I.G. 691 ; 4 I.T.C. 352.

Commissioner of Income-tax, Bombay v. Swarup Chand Hukumchand (1931) I.L.R. 59 Bom. 231 ; A.I.R. 1931 Bom. 236 ; 5 I.T.C. 108.

Croft v. Dunphy (1933) A.C. 156.

Dayaldas Kushiram v. Commissioner of Income-tax, Central (1940) I.L.R. 1940 Bom. 650 ; 8 I.T.R. 139 ; 42 Bom. L.R. 414 ; 3 F.L.J.H.C. 75.

De Beers Consolidated Mines Ltd. v. Howe (1906) L.R. 1906 A.C. 455 ; 5 Tax Cas. 198.

Dewarkhand Cement Co. Ltd. v. Secretary of State for India (1939) I.L.R. 1939 Bom. 320 ; 2 F.L.J.H.C. 60.

Forbes v. Secretary of State for India (1915) I.L.R. 42 Cal. 151 ; 19 C.W.N. 138 ; 26 I.C. 893 ; 1 I.T.C. 8.

Ford Motor Company of India Ltd. v. The Secretary of State for India in Council (1938) 65 I.A. 32 ; 172 I.C. 771 ; 1938 Bom. 249.

Gobindarajulu Naidu v. Secretary of State for India (1927) I.L.R. 50 Mad. 449 ; A.I.R. 1927 Mad. 689 ; 105 I.C. 576 ; 53 M.L.J. 355.

Gramophone and Typewriter Ltd. v. Stanley (1908) 2 K.B. 89 ; 77 L.J.K.B. 834 ; 99 L.T. 39 ; 5 Tax Cas. 358.

Haji Rahamatulla v. Secretary of State for India in Council (1926) 92 I.C. 351 ; 2 I.T.C. 118 ; 27 Bom. L.R. 1507 ; A.I.R. 1926 Bom. 50.

Hodge v. The Queen (1883) L.R. 9 A.C. 117.

London & South American Investment Trust Ltd. v. British Tobacco Company (Australia) Ltd. (1927) L.R. 1927, 1 Ch. 107.

Macleod v. Attorney-General for South Wales (1891) A.C. 455.

Maskell v. Herner (1915) K.B. 105.

Raja of Ramnad v. Secretary of State (1929) I.L.R. 52 Mad. 12.

Rex v. Burah (1878) 3 App. Cas. 889 ; 5 I.A. 178.

Secretary of State v. Fahaminnessa Begum (L.R. 17 I.A. 40).

Secretary of State for India v. Forbes (1922) A.I.R. 1922 Pat. 361.

Secretary of State for India v. Mask & Co. (1940) L.R. 67 I.A. 222 ; 3 F.L.J. P.C. 15.

Secretary of State v. Meyyappa Chettiar (1937) I.L.R. 1937 Mad. 211.

Seth Kanhaya Lal v. The National Bank of India, Ltd. L.R. 40 I.A. 56.

Singha v. Secretary of State for India I.L.R. 5 Rang. 825.

Spooner v. Juddow (1845-51) 4 M.I.A. 353.

Swedish Central Ry. Co. v. Thompson (1925) L.R. 1925 A.C. 495 ; 94 L.J.K.B. 527 ; 133 L.T. 97 ; 41 T.L.R. 385.

Thia Yen v. Secretary of State for India (1939) A.I.R. 1939 Cal. 763 ; 187 I.C. 542 ; I.L.R. 1939, 1 Cal. 257 ; 3 F.L.J. H.C. 50.

Thyagaraja Chettiar v. Collector of Madura (1936) 4 I.T.R. 56 ; 70 M.L.J. 343 ; 163 I.C. 60 ; 59 Mad. 702 ; A.I.R. 1936 Mad 398.

Trustees, Executors and Agency v. Federal Commissioner of Taxation (49 Commonwealth Reports 220).

Vacuum Oil Company v. The Secretary of State for India in Council (1932) A.I.R. 1932 P.C. 168 ; 137 I.C. 335 ; 59 I.A. 258 ; 56 Bom. 313.

Valphy v. Manley (1 C.B. 594).

Wolverhampton New Water Works Co. v. Hakesworth (1859) 28 L.J.C.P. 242 ; 7 W.R. 464 ; 6 C.B.N.S. 236.

S. M. Bose, S. O. Isaacs and S. Mitra, for the Plaintiff.

Sir A. K. Roy, Advocate-General, P. C. Ghose, and P. Chakravarthi, for the Defendant.

Suit No. 533 of 1942.

JUDGMENT.

DERBYSHIRE, C.J.—This matter originally came before McNair, J., who referred it to the Chief Justice, under rule 3 of Chapter V of the Original Side Rules which is as follows :—

“Where it shall appear to any Judge at any stage of a suit, application or other matter, that it involves a substantial question of law as to the interpretation of the Government of India Act, 1935, or any Order in Council made thereunder, he shall report to that effect to the Chief Justice, who shall constitute a Bench of two or more Judges to hear the suit, application or other matter.”

Put shortly the plaintiffs claim that certain provisions of the Indian Income-tax Act of 1922 as amended by the Income-tax Act of 1939 are beyond the law-making powers of the Indian Central Legislature and that in consequence certain money they have paid under protest to the Government of India as income-tax under the said provisions was not legally payable by them; they claim a declaration that the said provisions are *ultra vires* and ask for a return of the money so paid and other reliefs.

The defendants in their written statement have pleaded Section 226 of the Government of India Act, 1935, which in its material part provides :

“No High Court shall have any original jurisdiction in any matter concerning the revenue, or concerning any act ordered or done in the collection thereof according to the usage and practice of the country or the law for the time being in force.”

In order to decide whether and to what extent this plea will avail the defendants it is necessary to go into the facts of the case and the relevant provisions of the law. There is no difference between the parties as to the facts.

The Governor-General in Council as representing the Government of India is a party to the suit and has appeared through Sir Asoka Roy, the Advocate-General of Bengal, not acting as the Advocate-General of Bengal, but as Counsel representing the Government of India; we were informed by Sir Asoka that it was not necessary to give special notice to the Government of India or the Advocate-General of India under Order XXVII-A of the Code of Civil Procedure as they were aware of the case and were represented by him.

The suit is brought by the Raleigh Investment Co., Ltd., a joint stock company incorporated under the English Companies Act, having its registered office at 13, Athol Street, Douglas, in the Isle of Man and its main office at Egham, Surrey, England. We are informed from the Bar that the reason for the company's registration in the Isle of Man

was to save registration fees. For all practical purposes it is an English company. It has no business premises in India, but holds the bulk of the shares in a number of companies which carry on the business of manufacturing and selling tobacco and cigarettes in India. These companies are as follows: (1) The Imperial Tobacco Company of India Ltd.; and (2) Carreras (India) Ltd. The two above companies which are referred to as "the rupee companies" are incorporated in India under the Indian Companies Act and have their registered offices and business headquarters at 37, Chowringhee, Calcutta, within the original jurisdiction of this Court. (3) The Arcadian Tobacco Co. Ltd.; (4) The Cigarette Manufacturers (India) Ltd.; (5) Dominion Tobacco Co. Ltd.; (6) General Advertising Agency (India) Ltd.; (7) Indian Leaf Tobacco Development Co. Ltd.; (8) Peninsular Tobacco Co. Ltd.; (9) Printers (India) Ltd.; (10) Thomas Bear & Sons (India) Ltd.; and (11) Tobacco Manufacturers (India) Ltd.

The Companies Nos. 3 to 11 inclusive are companies under the English Companies Acts and are referred to as "the sterling companies."

A statement was put in by the plaintiffs which is agreed by the defendants to be correct and it is as follows:

"The nine sterling companies are controlled in London where the Boards of Directors sit, the share registers are situate, and dividends are declared. The boards in London have constituted local boards which are situate in India. The business in India, where all profits are made, is managed by the local boards. The ultimate control lies with the London boards. No share registers are kept in India. The financial policy of the companies is controlled by the London boards, and in all important matters of business the London boards are consulted. All the general meetings of the companies are held in England. The registered offices of six of the sterling companies are in the Isle of Man and of three others in London, but all the sterling companies have offices in London."

Copies of Articles 97, 98 and 100 of the Memorandum of Association of the Tobacco Manufacturers (India) Ltd., are exhibited separately. It is agreed that each of the other sterling companies contains similar Articles. These are marked Exhibit B.

All the companies above concerned, with the exception of the plaintiffs, have carried on business in India and made profits here which have been assessed to income-tax and super-tax under the Indian Income-tax laws and those taxes have been paid. Dividends have been declared after payment of Indian income-tax and super-tax by the 11 companies, and the plaintiffs have received such dividends as they

are entitled to on their share-holdings in those eleven companies. Dividends on the two rupee-companies were paid to a representative of the plaintiff company at 37, Chowringhee, Calcutta. The dividends of the nine sterling companies were declared by them in England and paid by them in England to the plaintiff company in England.

On June 6, 1939, the Income-tax Officer, Companies District III, 3, Government Place West, Calcutta (which is within the jurisdiction of the Original Side of this Court) sent to the plaintiffs a notice under Sections 22 (2) and 38 of the Indian Income-tax Act of 1922, as follows :

" 1. In pursuance of the provisions of Section 22 (2) of the Indian Income-tax Act, 1922, you are hereby required to prepare a true and correct statement of the company's total income and total world income during the previous years in the attached form along with such other particulars as are required to complete the form) and to deliver it to me at my office duly signed by you on behalf of the company on or before 12-7-1939 or within 30 days of the receipt of the notice (should the former date be less than 30 days after the receipt of the notice).

2. The form contains the instructions required for the preparation of the return. If you desire any further information, you should apply to this office.

A separate form for making this return is annexed."

That notice was addressed to the Raleigh Investment Co. Ltd., at 37, Chowringhee, Calcutta. The plaintiffs have no business premises in India, but the notice was forwarded by someone at 37, Chowringhee to the plaintiffs in England who made a return signed by their Secretary on August 18, 1939, giving their address as " Westminister House, 7 Millbank, London S.W. 1." That return apparently was sent by the plaintiffs from London to 37, Chowringhee, Calcutta, from which address it was forwarded on August 25, 1939, to the same Income-tax Officer by one A. S. McAra with the following covering letter :

" Dear Sir,

At the request of the Raleigh Investment Co. Ltd. I pass on to you herewith their return under Section 22 in respect of the income-tax year 1939-40."

On September 11, 1939, the same Income-tax Officer wrote to the plaintiffs at 37, Chowringhee, a letter with regard to the assessment for 1939-40 asking to be furnished with certificates under Section 20 in respect of dividends received during the year ending March 31, 1939. There was further correspondence in which on each occasion the Income-tax Officer addressed the plaintiffs at 37, Chowringhee, Calcutta, and eventually obtained replies through 37, Chowringhee, Calcutta.

On April 3, 1940, the Income-tax Officer wrote a letter to the plaintiffs—c/o Messrs. Imperial Tobacco Co. of India Ltd., 37, Chowringhee, Calcutta. Paragraph 6 of this letter is as follows:

“You are further requested to let me know that in view of Explanation (3) to Section 4 (1) of the Act, the dividends shown in Section D of the return being income accruing or arising in British India and thus liable to be included in total income, it appears that the total income accruing or arising in British India exceed the income arising without British India in the previous year and as such in terms of Section 4-A (c) the company is to be treated as resident in British India and as such the entire profits are liable to be taxed.”

(the letter is reproduced as put in evidence, the wording is faulty.) Paragraph 7 is as follows:

“You are requested to let me know if you have anything to urge against this.”

On June 3, 1940, the plaintiffs replied from Rusham House, Egham, Surrey, to which address they had apparently removed from Millbank, London, as follows:

“Dear Sir,

Your letter of the 3rd April, addressed to this company, care of the Imperial Tobacco Company of India, Limited, Calcutta, has been forwarded to us.”

The Company contends that dividends declared outside British India are not income accruing or arising in British India on the following grounds:—

(a) Explanation (3) to Section 4 (1) of the Indian Income-tax Act, 1922, as amended by the Indian Income-tax Amendment Act, 1939, on its true construction refers to dividends declared within British India but paid outside British India, and not to dividends declared outside British India.

(b) Alternatively, if on its true construction the said Explanation refers to dividends declared outside British India the Explanation is *ultra vires* the Central Indian Legislature which is not empowered under the Government of India Act, 1935, to impose a tax on persons not resident in British India in respect of income which does not arise in British India. Dividends declared outside British India are debts arising outside British India.

It follows that the company cannot be treated as resident in British India as the dividends shown in Section C of the Return are not income accruing or arising in British India and cannot be deemed so to accrue or arise, and in consequence, the income of the company arising

in British India (shown in Section A of the return) does not exceed its income arising outside British India.

The above deals with paragraphs 1, 2, 6 and 7 of your letter. As regards paragraph 3, I would confirm that Vazir Sultan Tobacco Company and London and Burma Tobacco Company Ltd., are not assessed to tax in British India.

In reply to paragraph 4 of your letter, the direct profits represent income other than dividends which arose from business carried on outside British India.

Copies of certificates where income-tax has been deducted from dividends shown in Section C of the Return asked for under paragraph 5 of your letter, are enclosed herewith, together with profit and loss account requested to be furnished under paragraph 8.

Nothing arises under paragraph 9 as this company has no representative in India."

The contention in paragraph 6 of the letter of the Income-tax Officer dated April 3, 1940, that "the total income accruing or arising in British India exceeds the income arising without British India in the previous year and as such in terms of Section 4-A (c) the Company is to be treated as resident in British India and as such the entire profits are liable to be taxed" has since been dropped.

It is convenient here to set out Section 4 (1) (c) of the Act and Explanation (3) which were added to the Indian Income-tax Act of 1922 by the Indian Income-tax (Amendment) Act of 1939 :

"4. (1) Subject to the provisions of this Act, the total income of any previous year of any person includes all income, profits and gains from whatever source derived which—

(c) if such person is not resident in British India during such year, accrue or arise or are deemed to accrue or arise to him in British India during such year."

Explanation is as follows :

"A dividend paid without British India shall be deemed to be income accruing and arising in British India to the extent to which it has been paid out of profits subjected to income-tax in British India."

At this time communications between India and England had become more difficult.

On August 2, 1940, the Income-tax Officer sent another notice under Section 22 of the Income-tax Act to the plaintiffs, and on August 3, Mr. Hamilton, an Accountant of the Imperial Tobacco Company of India, Ltd., at 37, Chowringhee, informed the Income-tax Officer of the difficulty in getting a reply from the Raleigh Investment Company, Ltd., and asked for an extension of time up till October 31, 1940.

On August 6, the Income-tax Officer replied to the Accountant extending the time for the submission of the return to November 4, 1940.

On September 13, the plaintiffs from England wrote to the Income-tax Officer direct adding another plea of *ultra vires*.

On October 15, the plaintiffs wrote from England direct to the Income-tax Officer, who received the letter on December 17, furnishing further returns in respect of Printers (India) Ltd.

On December 23, 1940, the Income-tax Officer made an assessment upon the plaintiffs of Rs. 72,047/ in respect of income-tax and Rs. 8,73,155-13-0 in respect of super-tax. These assessments were as follows: "The Raleigh Investment Company, Ltd., received the following dividends—

| | | | |
|-----------------------|------------|---------------|-----------------|
| From Imperial Tobacco | on 30-9-38 | Net. | Gross. |
| Co. of India, Ltd. | & 29-3-39 | Rs. 11,58,000 | Rs. 13,57,086 |
| Carreras (India) Ltd. | In Sep. 39 | „ 1,25,000 | „ 1,46,490 |
| | and | | |
| | March 39 | | Rs. 15,03,576." |

(The net amounts referred to are net amounts of dividend paid by the rupee-companies to the plaintiffs after deducting the income-tax and super-tax which the two rupee companies had paid on their profits: the gross amount is the amount of the net together with income-tax and super-tax paid by each rupee-company added back. The dividends paid by the sterling-companies to the plaintiffs amounted to £3,86,648-19-7 equivalent to Rs. 51,55,307/-. The income-tax and super-tax already paid by these companies on their profits in India was Rs. 8,86,314/-. This was added to the Rs. 51,55,307/- giving a total for Indian income-tax purposes of dividend received from the sterling-companies of Rs. 60,41,621/-. There was therefore a grand total for purposes of assessment of Rs. 75,45,197/-.) Upon that the plaintiffs were assessed as follows:

| | | | |
|--------------------------|---------------|--------------|-----------------|
| " Total income | Rs. 75,45,197 | | |
| Income-tax @ 30 pies | „ 11,78,937 | | |
| Tax paid Rs. 8,86,314 | | | |
| 2,20,576 | „ 11,06,890 | Rs. 72,047 | |
| Super-tax @ 12 pies | „ 4,71,574 13 | | |
| Deduct under Sec. 18 (3) | | | |
| On 5-5-39 Rs. 45,943 | | | |
| 19-4-39 | „ 5,951 2 | | |
| | „ 3,967 7 | | |
| | „ 42,557 9 | Rs. 98,419 2 | Rs. 3,73,155 13 |
| | | Total demand | Rs. 4,48,202 13 |

On the same day a copy of this assessment was sent by the Income-tax Officer together with a notice of demand under Section 29 of the Indian Income-tax Act to the plaintiffs at 37, Chowringhee, Calcutta. On January 2, 1941, Mr. McAra writing as a director of the Imperial Tobacco Company of India wrote back to the Income-tax Officer stating as follows :—

“Dear Sir,

On Friday or Saturday last week delivery of a cover addressed to the Raleigh Investment Co., Ltd., 37, Chowringhee, Calcutta, from your office was incorrectly accepted here.

You have already been advised that the Raleigh Investment Co. Ltd., have no place of business nor any representative in this country, and you were informed of the address to which correspondence should be sent.

We have, on this occasion and without accepting any responsibility as to the ultimate delivery, re-addressed and air-mailed the cover to England; but if the contents called for an urgent reply or laid down a time limit within which some action should be performed, we would remind you that there is very considerable delay in the transmission of mails between this country and the United Kingdom.”

On February 19, the plaintiff company from England telegraphed to the Income-tax Officer, Calcutta, intimating to him that they would appeal against the assessment and on February 21, the Income-tax Officer replied by telegram : “Appeal accepted if posted 19th March. Arrange payment by 15th March.” On February 24, 1941, the Income-tax Officer wrote to the Raleigh Investment Co. Ltd., in England as follows :—

“With reference to your cable dated 19th February 1941, I have the honour to enclose herewith a copy of computation of assessment for 1939-40 with the request to pay up the demand as early as possible.”

That was received by the plaintiffs on May 13, 1941. On February 28, the plaintiffs from London cabled the Income-tax Officer as follows : “Your cable 22nd requiring payment by 15th March. Are you prepared to exercise discretion under Section 45. Treat assessee as not in default whilst appeal undisposed of.”

On March 5, the Income-tax Officer cabled to the plaintiffs in England in reply : “Your cable 28th. Sorry cannot exercise discretion under Section 45. Arrange payment by 15th March.”

On or about March 12, 1941, the plaintiffs under protest remitted to the Income-tax authorities in Calcutta by telegraphic transfer

from England the amount of the assessment and demand, *viz.*, Rs. 4,45,202-13-0. The plaintiffs said that they paid the sum under protest in order to avoid penalties and other proceedings that might be taken against them as an assessee in default under the provisions of the Indian Income-tax Act.

There are various provisions in Section 46 of the Indian Income-tax Act under which the Income-tax authorities in India might have caused to be attached either the plaintiffs' share in the rupee-companies or the dividends payable to the plaintiffs on these shares. Doubtless the plaintiffs were afraid there might be such attachment unless they paid and of course they were minded to appeal against assessment. Such an appeal, dated March 11, 1941, when received in India was actually lodged by a Mr. Ryan, a solicitor of 37, Chowringhee, on or about June 4, 1941. In the grounds of appeal the plaintiffs raise substantially the same contentions as had been raised in the plaintiffs' letters of June 3 and September 13, 1940, which had been before the Income-tax Officer when he made the assessment. The Income-tax Officer, as the assessment shows, rejected paragraph (a) of the plaintiffs' objections in the letter of June 3. He did not deal with the question of *ultra vires*.

On August 21, 1941, Mr. Ryan wrote to the Appellate Assistant Commissioner of Income-tax as follows :

"In view of certain constitutional questions which are raised by some of the Grounds of Appeal in this case, the Raleigh Investment Co. Ltd., has been advised to take other proceedings to have those questions determined. What form those proceedings should take is now under consideration.

In the meantime, the Raleigh Investment Co. Ltd., does not wish to abandon its rights under the Act respecting the assessment on the constitutional questions or on the other grounds raised. In the circumstances, I request that you would be good enough to allow the appeal to remain in abeyance by adjourning it *sine die* until such time as the Raleigh Investment Co., Ltd., been (*sic*) able to decide upon its other course of action."

On November 11, 1941, the Appellate Assistant Commissioner wrote to Mr. Ryan as follows :

"The request in your letter of 21-8-41 is unusual and your proposed proceedings relating to the constitutional issues cannot arise under the Indian Income-tax Act under certain provisions of which I am to hear and decide the appeal. The procedure under this Act has to be followed. If I decide against you, you may go to the Appellate

Tribunal against whose order, if advised, you may ask for a Reference to the High Court. I do not propose therefore to keep the appeal in abeyance as you suggest and request you to let me know when Mr. Isaacs will be available in case you want him to appear at all.

On hearing from you I shall try to fix an early date but I am so heavily booked ahead for a long time that I cannot at this stage foresee the date. As Saturdays are High Court holidays, may not a Saturday, if possible this month, suit you and Mr. Isaacs?

On November 17, 1941, Mr. Ryan wrote back that Mr. Isaacs was busy and that he was awaiting instructions from England on the question of the appropriate procedure to be adopted by the assessesees. He appealed to the Appellate Assistant Commissioner not to fix a date for the hearing of the appeal before the middle of January.

The Appellate Assistant Commissioner replied by giving a notice on November 27 fixing January 17, 1942, for the hearing and final disposal of the appeal.

On December 16, 1941, the plaintiffs gave a written notice to the Secretary to the Central Board of Revenue of the Government of India, New Delhi, setting out the facts and stating that they intended upon the expiration of two months from that date to file a suit in the High Court at Calcutta, against the Governor-Général in Council claiming the reliefs which have now been claimed. This notice was given pursuant to Section 80 of the Code of Civil Procedure. On January 16, 1942, Mr. Ryan on behalf of the plaintiffs gave notice to the Appellate Assistant Commissioner in Calcutta that he did not propose to proceed with the appeal against the assessment under the Income-tax Act.

Under the provisions of the Indian Income-tax Act there is an appeal from the assessment by an Income-tax Officer to the Appellate Assistant Income-tax Commissioner under Section 30 of the Act, and from him to an Appellate Tribunal set up under Section 33 of the Act. The Appellate Tribunal consists of two members, one of whom has judicial experience and is generally an ex-District Judge whilst the other is an Accountant. The Appellate Tribunal may state a case for the opinion of the High Court under Section 66 of the Indian Income-tax Act. The High Court's functions with regard to such case stated are to advice on the law and from its judgment or opinion there is an appeal to the Privy Council.

On April 17, the plaintiffs began the present proceedings in this Court claiming :

(1) a declaration that in so far as Explanation 3 and the other provisions of Section 4 of the Indian Income-tax Act purport to authorise

the assessment and charging to tax of a non-resident company in respect of dividends which have been declared and/or paid outside British India upon shares situate outside British India but which have never been brought into British India, the said provisions are *ultra vires* the legislative powers of the Central Indian Legislature and that therefore the plaintiff company is not liable to be assessed or charged to income-tax or super-tax in respect of the said dividends of the sterling companies and that the said assessment for the year 1939-40 was illegal and wrongful;

(2) an injunction restraining the defendant, his officers, servants or agents from making any further assessment upon the plaintiff company in any subsequent years in respect of dividends of sterling companies declared and paid outside British India and not brought into British India;

(3) repayment of the said total sum of Rs. 4,35,290-5-0 as income-tax and super-tax illegally levied and/or as money paid under coercion or duress and/or as money had and received by the defendant to the use of the plaintiff company;

(4) interest upon the said sum of Rs. 57,689/- and Rs. 3,73,155-13-0 (portions of the said total sum of Rs. 4,35,290-5-0) under the Interest Act at the rate of 12 per centum per annum as from the 22nd December 1941 until judgment, and further interest from the date of judgment until payment upon the whole of the said sum of Rs. 4,35,290-5-0 at the rate of 6 per centum per annum or such other rate as may be allowed by this Court; and

(5) such further or other relief as the Court shall deem just.

Referring back to the assessment it will be noticed that the plaintiffs claim the return of Rs. 57,689/- instead of Rs. 72,047/- and Rs. 4,35,290-5-0 instead of Rs. 4,45,202-13-0 paid. The reason for this is that the plaintiffs do not question the right of the Government to tax them in respect of the rupee-companies' dividends which the plaintiffs received in India. We are, therefore, not concerned, in this case with the question of taxation of the dividends received from the rupee-companies. The sum of Rs. 57,689/- arises in this way: the dividends received by the plaintiffs from the two rupee-companies and the sterling-companies were taxed to income-tax under the Finance Act of 1938 at the rate of twenty-six pies per rupee and the total of the income-tax paid by the rupee-companies amounted to Rs. 11,06,890/-. The Government have taxed the plaintiffs in respect of the same amount of income when received by them at the rate of thirty pies per rupee under the Finance Act of 1939. This income-tax amounted to Rs. 11,78,937/-. Section 49B of the Income-tax Act provides:

“Where a shareholder has received a dividend from a company which has paid income-tax imposed in British India or elsewhere, he shall be deemed, in respect of such dividend, himself to have paid the income-tax (exclusive of super-tax) paid by the company on so much of the dividend as bears to the whole the same proportion as the amount of income on which the company has paid such income-tax bears to the whole income of the company.”

There is no similar provision in respect of super-tax which is a flat rate tax payable by companies as well as individuals. The consequence is that the Income-tax authorities gave the plaintiffs credit for the income-tax paid by the two rupee and nine sterling companies, *viz.*, Rs. 11,06,890/- against the income-tax demanded of the Raleigh Investment Company Ltd., *viz.*, Rs. 11,78,939/-. The difference is Rs. 72,047/- which is a part of the money the plaintiffs paid. Of that amount of tax a certain proportion is attributable to the dividend received from the rupee-companies about which there is now no dispute. The proportionate amount attributable to the sterling companies is Rs. 57,689/-.

As regards the item of Rs. 3,73,155-13-0 this is super-tax paid by the plaintiffs in respect of the income received by them from the rupee companies (Rs. 15,03,576/-) and the sterling companies (Rs. 60,41,621/-) in all Rs. 75,45,197/-). Each of the rupee companies and the sterling-companies had already paid super-tax on their respective profits at the flat rate before they paid their dividends to the plaintiffs.

Section 18 (3-D) of the Income-tax Act provides that an Income-tax Officer, if he has reason to believe that a non-resident shareholder would be liable to super-tax, may direct the principal officer of the company to deduct super-tax at the time of the payment of the dividend. Further under Section 18 (3-E) it is the duty of such principal officer, even if he receives no direction to deduct super-tax from the dividend payable to a non-resident shareholder, if the amount of such dividend is found to have reached the limit at which super-tax begins to be chargeable.

The rupee companies made this deduction before paying their dividends to the plaintiffs. The rate of super-tax in 1938 when the deduction was made was thirteen pies in the rupee. The rate of super-tax in 1939 when the plaintiffs submitted to payment of super-tax on their dividends from the rupee-companies was only twelve pies in the rupee. The result is that the plaintiffs were over-charged and made over-payment to the extent of Rs. 4,455-10-0. Credit is given for this in the assessment. As regards the sterling companies, although they were paying super-tax on their own profits in India, they

did not before declaring their dividends make any deduction under Section 18 (3-D) and Section 18 (3-E). The result is that the plaintiffs have been assessed on their income from the sterling companies (Rs. 60,41,621/-) to super-tax for the year 1939 to the amount of Rs. 3,77,601-5-0. Hence the net assessment of the plaintiff company for super-tax for the year 1939 was Rs. 3,77,601-5-0 less the credit from the rupee-companies' over-deduction of super-tax Rs. 4,455-10-0, that is, Rs. 3,73,155-13-0. All the profits and gains of the sterling companies in India had already been fully assessed and taxed to super-tax in India before the plaintiffs received their dividends from those profits. The defendants have taxed the plaintiffs and the plaintiffs have paid in all Rs. 57,689/- as income-tax together with Rs. 3,73,155-13-0 as super-tax under the defendants' assessment and demand, and their claim is to recover it. On the profits of the sterling companies on which taxes are levied, the proper taxes in India have been paid by the sterling companies before the dividends were declared by the sterling companies.

As this case may well go to other Courts which may wish to have details of these taxes explained to them I asked the Income-tax Authorities who were present in Court to be good enough to prepare a table with necessary explanations to show, how the taxes have been arrived at. The table and the explanations are exhibited and marked Exhibit 1.

The written statement put in by the defendant admits in paragraph 2 that the dividends of the sterling companies were declared, paid and received in England and that the plaintiffs were assessed on such a basis. In paragraph 3 the defendant pleads that—

“ The plaintiff company is the principal shareholder in all the rupee companies as well as the sterling companies referred to in paragraph 2 of the plaint. As such the plaintiff company controls the business and trade of all the said companies in British India. In any event the plaintiff company has sufficient interest in the capital and assets of the said companies employed in British India and in the trading operations of the said companies in British India to make it liable to Indian Income-tax in respect of income arising out of such trading operations.”

This plea has not been developed, but is I believe disposed of hereafter in this judgment. The defendant denies that the sums paid by the plaintiffs were paid under any coercion or duress. He also denies that provisions of Explanation 3 to Section 4 (1) of the Indian Income-tax Act are *ultra vires* of the legislative powers of the Central Indian Legislature as defined by the Government of India Act, 1935.

Lastly, in paragraph 11 of the written statement there is this plea :

“ The plaintiff company has no cause of action. In any event the defendant will object and contend that this Court has no jurisdiction to entertain this suit by virtue of Section 226 of the Government of India Act.”

Section 226 of the Government of India Act provides :

“(1) Until otherwise provided by Act of the appropriate legislature, no High Court shall have any original jurisdiction in any matter concerning the revenue, or concerning any act ordered or done in the collection thereof according to the usage and practice of the country or the law for the time being in force.

(2) A Bill or amendment for making such provision as aforesaid shall not be introduced into or moved in a Chamber of the Federal or a Provincial Legislature without the previous sanction of the Governor-General in his discretion or, as the case may be, of the Governor in his discretion.”

Defendant's Counsel in this case has argued very strenuously, under instruction of his client through the Central Board of Revenue, that Section 226 of the Government of India Act precluded us from entertaining this suit in any form. This attitude is strange in view of the fact that in two cases which intimately concerned the revenue the plea was apparently not raised. I refer to the case of the *Vacuum Oil Co. v. The Secretary of State for India in Council* reported in L.L.R. 56 Bom. 313 and the case of the *Ford Motor Company of India Ltd. v. The Secretary of State for India in Council* reported in L.R. 65 I.A. 32.

In each of these cases the plaintiffs under protest paid duty levied by the Customs Authorities at Bombay under the Sea Customs Act, 1878, and then brought proceedings in the High Court at Bombay to recover amounts of money which they claimed were illegally levied as duty upon their goods. In each case the suit was brought against the Secretary of State, who stood in the same position as the Governor-General does in this case, on the Original Side of the High Court in Bombay. The Vacuum Oil Company was successful in the Court of first instance, unsuccessful in the Appellate Court at Bombay and successful in the Privy Council. In the other case the Ford Motor Company were substantially unsuccessful in the Court of first instance and also on appeal to the Bombay High Court and in the Privy Council.

There is no evidence of any plea of Section 226 of the Government of India Act, 1935, or its predecessor Section 106 (2) of the Government

of India Act, 1915, being raised although Sea Customs Duty is just as much revenue as income-tax. However, the matter must be decided according to law.

This particular section, except where it provides for its repeal, substantially re-enacts Section 8 of the Act of Settlement, 1781. This section was enacted to prevent the Supreme Court in Calcutta from interfering with the East India Company's collection of land revenue. It has been retained in successive enactments and, in particular, Section 106 (2) of the Government of India Act, 1915.

It will be noticed that it is only the exercise of the original jurisdiction of the High Court that is forbidden. The exercise of the appellate jurisdiction of the High Court is not forbidden. Had the offices of the Income-tax Officer been two miles south of where they are now and so outside the ordinary original jurisdiction of this Court (which extends only to the limited part of Calcutta which is bounded by the Circular Road and the river Hooghly but contains the business part) the present proceedings would have been started before a Subordinate Judge in the Alipore Court which is in greater Calcutta and come to this Court to be dealt with on appeal without Section 226 being pleadable.

Both the plaintiffs' solicitors' office and the Income-tax Office where the money was paid are within the ordinary original jurisdiction of this Court.

Some very severe strictures have been passed by the High Courts in Bombay and Madras on the bar which Section 226 and its predecessors have raised to the original jurisdiction of the High Courts. I can only add my comment that its retention is an impediment to justice being had by those who reside or do business in the city of Calcutta. It is not in the interests of the subject and it is not in the real interests of the State. It has been used in the present case to hinder a British national who is not resident in India from obtaining a judicial determination of his rights.

It has been argued that the proper and only course for the plaintiffs to have taken to raise this matter was to appeal from the Income-tax Officer to the Appellate Assistant Commissioner, then to the Appellate Tribunal and then by way of a case stated to the High Court under Sections 66 and 66A of the Indian Income-tax Act.

It will be recollected that the plaintiffs raised the question of Section 4 (1) (c), Explanation (3), being *ultra vires* before the Income-tax Officer who did not deal with it but made the assessment. It will be remembered that Mr. Ryan on August 21, 1941, mentioned this constitutional question to the Appellate Assistant Commissioner and stated

that the form of the proceedings to raise it was under consideration and asked for an adjournment. The Appellate Assistant Commissioner replied: "Your proposed proceedings relating to the constitutional issues cannot arise under the Income-tax Act under certain provisions of which I am to hear and decide the appeal."

I think the Appellate Assistant Commissioner, although he, like the Income-tax Officer, is not a lawyer, realised that in giving a decision on the validity of Section 4 (1) (c), Explanation (3), he would be going beyond both his authority and legal capacity. He was employed to administer the Act and he had to take the Act as he found it. Section 30 (1) says :

"Any assessee.....denying his liability to be assessed under this Act.....may appeal to the Appellate Assistant Commissioner."

In that appeal both parties had to take the Act as they found it, not the Act with Explanation (3) of Section 4 (1) (c) treated as in doubt. It appears to me that the Appellate Tribunal, although one of the two members of it is a gentleman with judicial experience, must take the Act as they find it and not call it in question.

Section 66 provides that within sixty days of the date on which he is served with a notice of an order under Section 33 (4) the assessee or the Commissioner may require the Appellate Tribunal to refer to the High Court any question of law arising out of such order.

I doubt whether the validity of Explanation (3) to Section 4 (1) (c) would arise out of the order. Moreover raising that question in a reference would present the Court with serious difficulties since it would not have evidence before it but only a statement of facts. If a constitutional question of this sort is to be raised it ought to be raised before a court which can bring every available fact before it to consider the matter in question in the proper way. From the decision of the High Court, as Section 66A (2) provides :

"An appeal shall lie to His Majesty in Council from any judgment of the High Court delivered on a reference made under Section 66 in any case which the High Court certifies to be a fit one for appeal to His Majesty in Council."

Section 66A was amended in 1938 after the Government of India Act had been passed. No provision has been made in it for an appeal to the Federal Court. Under Section 205 of the Government of India Act it is provided that an appeal shall lie to the Federal Court from a judgment of a High Court if the High Court certifies that the case involves a substantial question of law as to the interpretation of the Government of India Act, 1935, and it shall be the duty of every High Court to consider in every case whether any such question is involved,

and on its own motion give or withhold a certificate accordingly. Section 205 (2) provides :

“ Where such a certificate is given, any party in the case may appeal to the Federal Court on the ground that any such question as aforesaid has been wrongly decided.....and no direct appeal shall lie to His Majesty in Council, either with or without special leave.”

In the present case a very important question as to the law-making powers of the Government of India under Sections 99 and 100 and List I, Item 54, of Schedule VII of the Act is involved. It is therefore imperative that the appeal from the High Court should be to the Federal Court.

It would seem therefore that appeals from High Courts in cases involving questions of law as to the interpretation of the Government of India Act, 1935, cannot go direct to the Privy Council but must go first to the Federal Court, and as appeals from judgments in references under Section 66 of the Income-tax Act must go to the Privy Council and not to the Federal Court, and as this matter involves basically a decision upon a substantial question of law as to the interpretation of the Government of India Act, 1935, a suit at law and not a reference under Section 66 of the Income-tax Act is the proper procedure.

The plaintiffs' claim in this suit is first to have Explanation (3) to Section 4 (1) (c) together with the relevant words of Section 4 (1) (c) declared invalid, and then the return of the money they have paid together with other connected reliefs. A decision in this suit will clearly affect the amount of money the Government will be able to collect as income-tax both in the year in question and in subsequent years. The suit would therefore appear to be one “ concerning the revenue.” It is necessary however to consider what the word “ revenue ” means. In 1781, when prohibition against the Supreme Court exercising original jurisdiction in matters concerning the revenue was first introduced into the Act of Settlement, revenue clearly meant income from land, but in 1935, when the same provision was substantially re-enacted, revenue, in view of the provisions of Sections 136 and 138 of the Act of 1935, would clearly include money derived from income-tax.

In the present case the plaintiffs say that the money they have paid as a result of the assessment and demand for income-tax is demanded under an invalid provision of law and therefore the money is not money paid under the law but is an illegal exaction.

If the money is not income-tax money but an illegal exaction it is money to which the Government of India has no legal claim or legal right and in that event it is money which the Government of India ought to repay to the plaintiffs. Is such money revenue ? The *Concise*

Oxford Dictionary defines "revenue" to be: "The state's annual income from which public expenses are met." Such definition accords very clearly with the ordinary conception of revenue.

In the present case the money the plaintiffs paid went into the Government's revenue account about March 15, 1941. In that sense it was, when paid, revenue, as would be all similar subsequent payments when made. As the relevant financial year ended on March 31, 1941, that money in all human probability would have been spent by April 17, 1942, when its return was claimed in this suit. On April 17, 1942, the money was strictly speaking no longer revenue. Whatever the position of this money on April 17, 1942, if it was demanded and obtained without any legal authority, it is the Government's duty to refund it or its equivalent which is the same thing. However, be that as it may, in the present case the Court is concerned with the legal rights and liabilities of the parties and therefore in my opinion the word "revenue" in Section 226 of the Government of India Act, 1935, must be taken to mean what is revenue according to law or shortly "legal revenue" and not illegal exactions.

Thus, before it can be decided that Section 226 of the Government of India Act, 1935, is a bar to the Court's jurisdiction, the Court must decide whether the money the plaintiffs paid was tax imposed under legal authority or illegal exaction. If the money was paid as a result of a demand for income-tax legally imposed, the Court can exercise no original jurisdiction concerning it in a suit. If the money was paid as the result of a demand made without legal authority the money is money illegally obtained and held to the use of the plaintiffs and there is no bar under Section 226 to our exercising original jurisdiction concerning it in this suit, nor under Section 67 of the Indian Income-tax Act.

In order to decide whether the money has been demanded and paid legally the Court must first determine whether the impugned legislation is valid or not. The Court is bound to enquire into and decide this matter to ascertain whether it has jurisdiction or not. Section 99 (1) of the Government of India Act provides: "Subject to the provisions of this Act, the Federal Legislature may make laws for the whole or any part of British India or for any Federated State." Federation is not yet in being but the Indian Central Legislature has meanwhile the same law-making powers as those given by the Act to the Federal Legislature: Section 316 of the Act. Section 99 (2) of the same Act provides:

"Without prejudice to the generality of the powers conferred by the preceding sub-section, no Federal law shall, on the ground that it would have extra-territorial operation, be deemed to be invalid in so far as it applies—

(a) to British subjects and servants of the Crown in any part of India; or

(b) to British subjects who are domiciled in any part of India wherever they may be; or

(c) to, or to persons on, ships or aircraft registered in British India or any Federated State wherever they may be; or

(d) in the case of a law with respect to a matter accepted in the Instrument of Accession of a Federated State as a matter with respect to which the Federal Legislature may make laws for that State, to subjects of that State wherever they may be; or

(e) in the case of a law for the regulation or discipline of any naval, military or air force raised in British India, to members of, and persons attached to, employed with or following, that force wherever they may be."

Section 100 provides that the Federal Legislature has power to make laws with respect to any of the matters enumerated in List I of the VIIth Schedule.

Item 54 of List I reads: "Taxes on income other than agricultural income."

Summing up the Indian Central Legislature's relevant powers in 1939 under Sections 99 (1), 100 and Item 54 of List I, they were: "to make laws for the whole or any part of British India with respect to taxes on income other than agricultural income."

Prima facie such laws could have no operation outside British India but Section 99 (2) provides that in certain specified cases in respect of certain specified classes of persons in certain areas outside British India either specified or indicated those laws may operate:

(1) as far as British subjects and servants of the Crown are concerned in any part of India;

(2) as far as British subjects domiciled in India are concerned, wherever they may be;

(3) as far as persons on ships or aircraft registered in British India wherever they may be;

(4) as far as members of and persons attached to or employed with or following naval, military or air force raised in British India, they may be subject to laws passed by the Indian Legislature to regulate or discipline them, wherever they may be.

Again in List I of Schedule VII there are the following matters on which the Government of India may legislate:

Item 3. Extradition and expulsion of criminals and other persons to parts of His Majesty's dominions outside India;

Item 22. Declaration and delimitation of ports;

Item 23. Fishing and fisheries beyond territorial waters ;

Item 24. Regulation and organisation of air traffic ;

Item 25. Lightships, beacons and other provisions for the safety of shipping and aircraft.

All these matters contemplate the making of laws which may in some events and to some extent be operative beyond British India.

It is difficult to state the precise effect of the words in Section 99 (2) "without prejudice to the generality of the powers conferred by the preceding sub-section....." They are however clearly precautionary and probably mean that laws made for British India, even when they do not come within the cases set out in Section 99 (2), may in certain eventualities which are either too numerous or uncertain to specify, have some extra-territoriality ; such as in the cases prescribed for in Items 3, 21, 23, 24 and 25 of List I, or where anti-smuggling laws are made as related in *Croft v. Dunphy*¹. There may be other such cases.

Such extra-territoriality would be of the kind and degree necessary to give efficacy to the legislation as it affected British India—small extensions for such purpose, perhaps into no-man's air or water, or perhaps by agreement with a neighbouring State into that State ; all other valid extra-territorial legislation must come within Section 99 (2) (a), (b), (c), (d) and (e).

In *Croft v. Dunphy*^a Lord Macmillan said : "Where a power is conferred to legislate on a particular topic it is important in determining the scope of the power to have regard to what is ordinarily treated as embraced within that topic in legislative practice and particularly in the legislative practice of the State which has conferred the power."

In Vol. 47 of the 2nd edition of *Halsbury's Laws of England* which deals with English Income-tax law as at April 1, 1935, just before the Government of India Act, 1935, was passed, there is this statement of the English Income-tax Law, at page 11 :

"The income arising abroad to non-resident is not within the charge to tax, and non-residents also enjoy specific exemption in certain cases (set out in footnote :—interest and dividends of a foreign State or British possession payable in the U. K. through a paying agent)."

It therefore appears that when the Government of India Act, 1935, was passed it was not the legislative practice of Great Britain to tax non-residents upon income received from outside the U. K. or in certain cases from inside the U. K.

(1) (1933) A.C. 156 at pp. 165-167.

As regards the position in British India in 1935 Sir Asoka Roy for the Government of India referred the Court to Section 42 of the Indian Income-tax Act prevailing at the time. It provided as follows:

"In the case of any person residing out of British India, all profits or gains accruing or arising to such person, whether directly or indirectly, through or from any business connection or property in British India, shall be deemed to be income accruing or arising within British India, and shall be chargeable to income-tax in the name of the agent of any such person, and such agent shall be deemed to be, for all the purposes of this Act, the assessee in respect of such income-tax :

Provided that any arrears of tax may be recovered also in accordance with the provisions of this Act from any assets of the non-resident person which are, or may at any time come, within British India."

This section provided for the assessment and taxation of the foreigner's India agent, and I doubt if it is extra-territorial in its effect.

The position as regards extra-territorial taxation of a foreigner was considered by the Bombay High Court in 1931 in the case of the *Commissioner of Income-tax, Bombay v. Goldie*¹, where the Indian Income-tax Authorities attempted to assess a non-resident person in respect of dividends declared in England by companies registered in England but doing business in India. The Court held that the non-resident was not so taxable.

It appears therefore that in 1935, legislation in India did not tax non-residents on income received abroad from companies registered in England although those companies traded in India. Indeed, had such been the position, the present legislation now objected to would probably not have been passed by the Indian Income-tax Amendment Act, 1939.

Reference to the legal position with regard to this matter in England and in India in 1935 does not mean that the Income-tax law in India after 1935 is to remain unchanged and unchangeable, but it does lend some support to the view that where the British Government had refrained from extra-territorial legislation involving taxation of non-residents upon income received by them abroad, it did not in the absence of express enactment intend to confer such power upon the Indian Government by the Act of 1935. Extra-territorial legislation is apt to produce friction between States and this is certainly so where one State taxes another State's nationals as Lord Esher pointed out in *Colquhoun v. Brooks*². The reactions to the assessment and demand for tax might have been much different in the present case had the plaintiffs been an American Company instead of a British Company.

(1) (1931) I.L.R. 55 Bom. 734,

(2) (1889) 21 Q.B.D. 57.

The dividends in respect of which tax has been claimed and paid in the present case were all dividends declared abroad by foreign Companies with registered offices, head offices and share registers either in England or in the Isle of Man (and were payable and paid either in England or in the Isle of Man) to the plaintiffs, a company registered in the Isle of Man with its head office in England. The dividends concerned were therefore debts arising abroad and paid abroad by Companies resident out of British India to the plaintiffs, another Company resident out of British India : see *London and South American Investment Trust Ltd. v. British Tobacco Company (Australia) Ltd.*¹

The effect of the words in Section 4 (1) (c) "or are deemed to accrue or arise to him" combined with Explanation (3) "a dividend paid without British India shall be deemed to be income accruing and arising in British India to the extent to which it has been paid out of profits subjected to income-tax in British India" is, as the facts of the present case show, to make liable to tax in British India foreign money measured in a foreign currency paid in a foreign country by one foreign Company to another foreign Company in discharge of a debt which arose and was payable in that foreign country. The condition attached "to the extent to which it has been paid out of profits subjected to income-tax in British India" does not make the money any less foreign money nor does it alter the nature or incidents of the debt. Further the money in question sought to be taxed was derived from the whole of the sterling dividend paying Companies' operations and not from any particular part of them.

Again, if in law the money sought to be taxed could by Explanation (3) to Section 4 (1) (c) be attributed to a source in British India, that money is the foreign exchange equivalent of money which has (as the Explanation postulates) been already subjected to tax in British India and therefore was received by foreign dividend paying Company free from liability to tax in British India.

The provision in Section 4 (1) (c) and the Explanation which is impugned is not legislation within the extra-territorial powers given in Section 99 (2) of the Government of India Act since its operation is not limited to the persons and places named in Section 99 (2); it is not legislation dealing with any of the matters mentioned in the Lists of Schedule VII in which some degree of extra-territorial legislation may be assumed were necessary to give efficacy to legislation for British India; it is something beyond all these.

This is a case of the Legislature of British India without specific or apparent authority stretching out its legislative arm and fiscal hands

(1) (1927) 1 Ch. 107.

beyond British India into other countries in an attempt to tax persons and property there not subject to its laws. In my opinion, for the reasons given above, the legislation impugned is not authorised by any provision, either express or implied, of the Government of India Act, 1935, from which statute the legislature of British India in 1939 derived its powers. I am therefore of opinion that the impugned legislation was and is beyond the law-making powers of the Government of India and therefore invalid. Consequently the words "or are deemed to accrue or arise" in Section 4 (1) of the Indian Income-tax Act and Explanation (3) thereof are of no legal effect.

The Government of India were only able to obtain the money now claimed in this suit from the plaintiffs because they were in a position to treat, and intended to treat, plaintiffs as defaulters under the Income-tax Act and so collect the money with possible penalties under the provisions of Section 46 of the Act if the plaintiffs did not pay. The plaintiffs had good reason to believe that their property, *i.e.*, the dividends from the rupee-companies in India, would be taken from them or from the companies that were due to pay money to them in India, if they did not yield to the Income-tax Officer's illegal demand. In my view the plaintiffs were in the same position as the plaintiff in the case of *Maskell v. Horner*¹ where the plaintiff Maskell sold his goods in Spitalfields Market and had a demand made upon him by the defendant for tolls under the threat of seizure of his goods if he refused to pay. Maskell objected to pay and seizure took place. Maskell then consulted a solicitor and upon learning that other dealers paid tolls he, acting upon his solicitor's advice, paid the tolls under protest and did so always thereafter. It was held that the circumstances of the payment and the conduct of the plaintiff throughout showed that he only paid to avoid seizure of his goods and never made payments voluntarily, or intended to give up his right to the sums paid, and that he was entitled to recover those tolls for a period of six years, the earlier payments being barred by the Statute of Limitation. In delivering judgment Lord Reading said:

"If a person pays money, which he is not bound to pay, under the compulsion of urgent and pressing necessity of seizure actual or threatened, of his goods, he can recover it as money had and received. The money is paid not under duress in the strict sense of the term, as that implies duress of a person, but under the pressure of seizure or detention of goods which is analogous to that of duress. Payment under such pressure establishes that the payment is not made voluntarily to close the transaction (per Parke, B., in *Atlee v. Backhouse*²). The

(1) (1915) K.B. 105.

(2) 3 M. & W. 633.

payment is made for the purpose of averting a threatened evil and is made not with the intention of giving up a right but under the immediate necessity and with the intention of preserving the right to dispute the legality of the demand (*per* Tindal, C. J., in *Valphy v. Manley*¹). There are numerous instances in the books of successful claims in this form of action to recover money paid to relieve goods from seizure."

At page 126 of the report Pickford, L.J., said :

"I do not think that the mere fact that a payment is made under protest is enough to entitle the payer to recover it back, but if it be shown that it was made under circumstances which show that the payer intends to resist the claim and yields to it merely for the purpose of relieving himself of the inconvenience of having his goods sold, the money can be recovered back, and the fact of a protest is some indication that it is so made."

It is inconceivable that the plaintiffs in the present case would under protest have paid money from England in the way they did over four lakhs of rupees—or in English currency over £ 30,000—to the Income-tax Officer in Calcutta but for the fact that the Income-tax Officer held threats of the Income-tax Act over their heads and the fear that he would use powers under Section 46 to take the plaintiffs' money coming from the rupee company whether they liked it or not.

Having found that the money now claimed was money paid by the plaintiffs to the Government of India as aforesaid as a result of a demand made under a law which the Government of India had no power to make and so an invalid law, I am of the opinion that the suit does not concern revenue in the sense used in Section 226, *viz.*, legal revenue, and that therefore the provisions of Section 226 of the Government of India Act do not bar our jurisdiction.

I am therefore of opinion that the plaintiffs are entitled to a declaration that the legislation impugned is invalid and to return of the money so paid, *viz.*, Rs. 4,35,290-5-0—money had and received—together with interest thereon at four per cent. per annum from the date of the notice of claim, *viz.*, December 21, 1942, until payment thereof.

MITTER, J.—The Raleigh Investment Company Limited, hereafter called the company, is a non-resident company. It is the principal shareholder in two companies, for brevity's sake called the rupee companies and in seven other companies, for brevity's sake called the sterling companies. We are not concerned in this suit with the assessment of the company to income-tax in respect of the dividends it had received from the rupee companies. The suit concerns only with the income-tax assessed on the dividend it received from the sterling companies.

(1) 1 C. B. 594 at 602.

The sterling companies are incorporated in England. Their principal place of business is in England where the share registers are kept. They carry on business operations in British India and other places. Dividends are declared in England. The dividends on which the plaintiff company has been assessed to income-tax here had been declared in England, paid to it in England, and no part of it had been brought into British India. It was assessed to income-tax by the Income-tax Officer, District C-III, Calcutta, on the basis of Explanation 3 to Section 4 of the Indian Income-tax Act, XI of 1922 (hereafter called the Act), on the 23rd December, 1940, for the financial year 1939-40. It preferred an appeal on the 6th June 1941, to the Appellate Assistant Commissioner under Section 30 of the Act, but did not proceed with the appeal which was dismissed for default on the 17th January, 1942.

The Income-tax Officer served a demand notice on the company requiring payment of the tax by the 15th March, 1941. The company on getting the same cabled to the Income-tax Officer from England on the 28th February, 1941, before filing the appeal, for postponement of the payment of the tax till the disposal of the proposed appeal and requested the latter not to treat it in default while the appeal would be pending. The cable was received by the Income-tax Officer on the 4th March, 1941, who sent a reply by cable on the same date expressing regret, and at the same time asked the company to arrange for payment by the 15th March, 1941. The money was paid by that date. This suit was filed by the company on the Original Side of this Court in April, 1942.

On the pleadings the following five issues have been raised :

1. Has the company any cause of action ?
2. Is the suit barred by reason of the provisions of the Indian Income-tax Act ?
3. Has this Court, in the exercise of its original jurisdiction, power to entertain the suit in view of Section 226 of the Government of India Act, 1935 ?
4. Is Explanation (3) to Section 4 of the Income-tax Act *ultra vires* the legislature ? and
5. What relief, if any, is to be given to the company ?

I would take up the fourth issue first.

The charging provisions (Sections 3 and 4) of the Income-tax Act before its amendment by Act VII of 1939 were as follows :—

A person whether residing in or outside British India in the relevant year, was chargeable only in respect of the income (a) which had arisen or accrued to him in the accounting year in British India or (b) which

had been received by him in British India. In the case of a resident only income which had arisen or accrued outside British India was to be *deemed*, subject to some limitations, to have arisen or accrued to him if it was either received or brought into British India. A non-resident could not have been assessed to tax on income which had arisen or accrued outside British India or income received outside British India even though it may have subsequently been brought into British India. The sentence "arises or accrued or received" etc., occurring in sub-section (1) of Section 4 was construed disjunctively. By the amending Act of 1939 Section 4 was in the first place re-arranged. Effect was given to the decisions under the old Act to the effect that two separate ideas had been expressed in sub-section (1) of Section 4, the phrase "arise or accrue" connoting one idea and the word "received" another distinct idea. The liability to be taxed on income received or deemed to have been received in British India was put under a separate clause (clause (a)) which means that the liability on the ground of receipt in British India would be on a person, be he a resident or non-resident. We are not concerned with that case. The section then places the assessee under two categories: (1) when he is a resident in British India and (2) when he is not: (clauses (b) & (c)). With regard to residents the general provision is that he is to be assessed on income which had not only arisen or accrued in British India or was deemed to have arisen or accrued in British India but also on income which had arisen or accrued outside British India. With regard to non-residents, however, they can be assessed on income which had arisen or accrued in British India or which is deemed to have arisen or accrued in British India. Explanation (3) to Section 4 which concerns dividends only includes the case where the dividend which did not in fact accrue to a person in British India is deemed to have accrued to him in British India, if it was paid out of profits (and to the extent thereof) of the company in which the dividend producing shares were held if those profits had been subject to income-tax in British India. Whether Explanation (3) is a good piece of legislation in reference to a person who is a resident in British India we are not called upon to decide, for in the case before us the plaintiff is a non-resident company. Income which in fact had arisen or accrued to a non-resident outside British India is brought within the British Indian assessment by this Explanation, for dividend which accrues to a share-holder of a company is income which is quite distinct from the income of the company in which the shares are held, even when the whole of the share capital of the company is held by that share-holder. This follows from the observations of Fletcher-Moulton, L. J., in *Gramophone and*

*Typewriter Ltd. v. Stanley*¹ and of Lord Wrenbury in *Bradbury v. English Sewing Cotton Co.*² The property of a person who may be the subject of another independent foreign State and may be a resident of such a State, and over whom the Indian Legislature has no jurisdiction is thus brought under the provision of a taxing statute enacted by the British Indian Legislature. Limiting Explanation (3) to the case of a non-resident, that explanation is a piece of extra-territorial legislation, not by a supreme or paramount legislature but by a subordinate legislature, which derives its authority from Parliament under the Government of India Act, 1935. The question is whether the explanation so far as it affects non-residents is *ultra vires* the Indian Legislature. The powers of the Indian Legislature during the transitional period are defined in Sections 99 and 100 of the Government of India Act, 1935. Item No. 54 of List I of the Seventh Schedule to that Act is "tax on income other than agricultural income." The subject accordingly falls within the field of legislation by the Indian Legislature.

Under the Government of India Act, 1915, the jurisdiction of the Indian Legislature to legislate was defined specifically. Subject to some exceptions not material for this case, it had power to legislate for all persons and things *within* British India (Section 65 clause (a)). The Government of India Act, 1935, contains no provision exactly similar to Section 65 (a). Section 99 (1) read with Section 100 of the Act of 1935 authorizes the Federal Legislature (Indian Legislature, during the transitional period: Section 316) to legislate for the whole or any part of British India in respect of the subjects specified in Lists I and III of the Seventh Schedule. Sub-section (2) of Section 99 expressly gives it power to legislate extra-territorially over some classes of persons. In respect of item No. 23, and it may be, No. 21 of List I, also the same power exists. That being the position we are to see whether in respect of income-tax the Indian Legislature has power to legislate extra-territorially. In my judgment that question must be answered on general principles keeping at the same time in view the provisions of Section 99.

The Imperial Parliament, being a sovereign legislature, is not subject to any restraint so far as concerns municipal laws. Its power and jurisdiction is so transcendent and absolute that it cannot be confined either for causes or persons within any bounds. According to International Law, however, it is not competent to the British Parliament to enact laws for foreigners out of the British Dominions and beyond jurisdiction or for vessels on the high seas or foreigners beyond the Empire. But if such a statute is passed, the domestic courts—the Courts

(1) (1908) 2 K.B. 89.

(2) (1923) A.C. 744 ; 8 Tax Cas. 481.

of the British Isles, of the Dominions and of the Empire—are bound to obey and administer them, it being left to the Government to justify its action with other countries diplomatically. It is a foreign question altogether how far the domestic courts would be able to enforce their decrees or how far those decrees may be recognised by courts of foreign countries. A subordinate legislature is, no doubt, not an agent or delegate of the supreme legislature in respect of legislation on the permitted subject but has plenary powers: *Rez v. Burah*¹, *Hodge v. The Queen*². That does not necessarily imply that it can legislate on the permitted subject in an extra-territorial manner in the same way as the supreme legislature. If the judgment of Lord Macmillan in *Croft v. Dunphy*³ be considered in its entirety it cannot be said that his Lordship was laying down by the observations at page 163 of the report, that every subordinate legislature can legislate with extra-territorial effect on the permitted subject just as the Imperial Parliament, for on the next page he observes that a statute violating International Law passed by the Imperial Parliament cannot be challenged as *ultra vires* in a domestic court but such a statute passed by a subordinate legislature can be challenged as *ultra vires* in a domestic court on the ground that the Imperial Parliament must not be taken to have granted the power to enact such a statute to a subordinate legislature. In the early part of my judgment I have pointed out that Explanation (3) to Section 4 of the Indian Income-tax Act has the effect of drawing in income that may have accrued within the territories of another independent foreign State to a person who may be the subject of, and resident in, the territories of another independent foreign State. In my judgment the general principle is that a subordinate legislature can legislate only within its territorial limits (*Macleod v. Attorney-General for New South Wales*⁴) unless otherwise authorized by the Imperial Parliament, either expressly or by necessary implication. Such an authority has been expressly conferred on the Indian Legislature in matters mentioned in sub-section (2) of Section 99 and in some of the items of List I, as for instance item No. 23. Whether a power to legislate extra-territorially has been conferred by the Imperial Parliament on a subordinate legislature by implication has to be determined on certain considerations. Before, however, examining what those considerations should be, I may point out that the principle of interpretation expressed by the maxim *expressio unius exclusio alterius* cannot be invoked to construe a constitutional enactment, the provisions of which by the very nature of the subject must to a certain degree be worded in elastic

(1) (1878) 5 I.A. 178.

(2) (1883) L.R. 9 A.C. 117.

(3) (1933) A.C. 156.

(4) (1891) L.R. 1891 A.C. 455, at 458.

forms. I cannot therefore accept the argument advanced on behalf of the plaintiff company that the Imperial Parliament by specifying the subjects over which the Indian Legislature can legislate extra-territorially intended that over all other subjects it was not to have that power.

In deciding the question whether the power to legislate extra-territorially has been conferred on a subordinate legislature by implication the following are the material considerations :—

(1) the legislative practice on that subject in the mother country, *Croft v. Dunphy*¹,

(2) the legislative practice in the territory subject to the jurisdiction of the subordinate legislature at or before the Constitution Act under consideration, *Byramjee Jeejeebhoy v. Province of Bombay*² also *In re Central Provinces and Berar Sales of Motor Spirit and Lubricants Taxation Act, 1938*³, and

(3) nature of the subject-matter of legislation.

In considering the nature of the subject-matter of legislation in reference to the question now before us the guiding principle is that “you can complement a given power but cannot supplement it.” If legislation on the permitted subject would not be effective without a provision being enacted having extra-territorial operation a power to legislate extra-territorially will be implied; for instance where the permitted subject of legislation is defence of the territory subject to the jurisdiction of the subordinate legislature, a provision in a statute which deals with that subject would not be considered *ultra vires*, because the provision has extra-territorial effect, the principle being that the Sovereign Legislature gave the subordinate legislature such a power by necessary implication. The absurdity of limiting the power to legislate within the territorial bounds in such a matter is well expressed by the phrase “Imagine the navy confined to the three mile limit.” The cases where the validity of laws of exclusion and expulsion passed by the Colonial or Dominion Legislatures were considered also fell within this category: (see *Attorney-General for Canada v. Cain and Gilhula*⁴).

The legislative practice in England in income-tax matters is summarised at pages 27 and 35 of Lord Macmillan’s Report (Income-tax Codification Report of 1936). According to the legislative practice in England a person who is a resident in the United Kingdom is charged upon the whole amount of his profits and gains whether they arose

(1) (1933) L.R. 1933 A.C. 156.

(2) (1940) I.L.R. 1940 Bom. 58, at 77; 7 I.T.R. 670; 3 F.L.J.H.C. 23.

(3) (1939) F.C.R. 18, at 53; 2 F.L.J. 6.

(4) (1908) L.R. 1906 AC. 542.

from property in the United Kingdom or elsewhere. The word "elsewhere" which ordinarily would include the rest of the earth outside the United Kingdom was by judicial decisions given a limited meaning. A person who is now a resident in the United Kingdom is charged only in respect of the profits derived from property situate within the United Kingdom. Lord Herschell summarised the law on the subject as in force in England in *Colquhoun v. Brooks*¹, thus:

"The Income-tax Acts themselves impose a territorial limit; either that from which the taxable income is derived must be situate in the United Kingdom or the person whose income is to be taxed must be a resident there."

In British India the first Income-tax Act was passed in 1860 (Act XXXII of 1860). Only persons resident in India were charged on annual profits arising from property whether situate in India or elsewhere and from trade, profession or employment whether the same was carried on in India or elsewhere. Non-residents, however, were charged only on profits of property situate in India and on profits of trade, profession, and employment carried on in India. Dividends and interest on money or securities were charged only if they were *payable* in India. The duration of the Act was for five years. The next Act, IX of 1868, was an Act which imposed tax on professions and trades carried on in India. It did not impose a tax on income but a tax in the nature of licence fees. The next two Acts (IX of 1869 and XVI of 1870) proceeded on same lines. Every office or employment of profit in British India and salaries, annuities and pensions paid in British India, the profits of shipping companies trading between British India and outside and profits of companies made in British India were taxed. By the Act of 1871 (XII of 1871) other incomes were brought in the field of taxation, but only the income which had accrued in British India was to be taxed. The next Act, II of 1886, made income which had arisen or accrued in British India or which had been received in British India or salaries paid to a British subject in the Native States by the Government of India or by a local authority could only be taxed. The Act of 1918 (Act VII of 1918) charged all income which arose, accrued or was received in British India or which under the provisions of that Act was to be deemed to have arisen, accrued or to have been received in British India. The only provision in that Act which defined what was to be deemed to have arisen etc. in British India was Section 33 which corresponds to Section 42 of the Act of 1922 (XI of 1922). The last mentioned Act, as it stood in 1935, and before the amendment of 1939, made the income of a resident taxable when the income had accrued, arisen or had been received in British India, or though arising out of

(1) (1889) L.R. 14 A.C. 493, at 504,

British India, has been received or brought into British India within a certain time, but with regard to a non-resident he could be taxed only in respect of income which had accrued or arisen in British India or which had been received there. The extending section was Section 42. The legislative practice in India up to 1935 was not to assess a non-resident who had no business connection in British India, to income-tax in respect of an income which had not arisen or accrued to him in British India or which had not been received by him in British India. Moreover the nature of the subject of legislation does not necessarily require any legislative provision of extra-territorial operation. I cannot therefore hold that the Indian legislature has been given by implication the power to legislate extra-territorially with regard to income-tax matters. Explanation (3) to Section 4 is accordingly *ultra vires* to the extent it relates to a non-resident who does not fulfil the conditions of Section 42 in respect of his income which did not in *fact* arise or accrue to him in British India. I refrain from making any observations with regard to any other case.

The two cases on which the learned Advocate-General has relied strongly are decisions of the Federal Court of Australia. They are *The Colonial Gas Association Ltd. v. Federal Commissioner of Taxation*¹ and *Trustees, Executors and Agency v. Federal Commissioner of Taxation*². The first case concerned income-tax and the second succession duty. I have not been able to secure the Australian Income-tax Act but from the summary of its provisions as made by Tomlin, J., as he then was, in *London and South British Investment Trust Co. Ltd. v. British Tobacco Co. Ltd.*³, and from Section 20 (2) (b) as quoted in the *Colonial Gas Association's case*¹ it appears that a company which carries on business in Australia is taxed by the Australian Statute on so much of its income which it does not distribute amongst its share-holders. The Company is also taxed on what it distributes as dividend to its members who are not residents in Australia, the company being given the right to deduct the tax from the dividend payable to non-resident share-holders. There is therefore no attempt to tax *directly* an absentee shareholder in respect of income which did not accrue to him in Australia. In the *Colonial Gas Association's case*¹, where the question was whether the amount paid to a non-resident debenture-holder could be taxed by the Australian Statute, Dixon, J., pointed out that the purpose of that statute was not dependent on the liability of the debenture-holders to pay income-tax to the Australian Government, but its purpose was to impose only upon such companies which derived assessable

(1) 51 Commonwealth Reports 172.

(3) (1927) L.R. 1927, 1 Ch. 107.

(2) 49 Commonwealth Reports 220.

income from Australia and on no others, an original or independent liability. The liability to the Crown was imposed on the company. No doubt the Australian legislature intended that the incidence of the tax should be ultimately on the absentee debenture-holder. This was sought to be effected by giving the company the right to deduct and retain the amount of tax payable by it on the interest payable to the absentee debenture-holder from the amount payable to them. Dixon, J., however stated in clear words that the company could not escape assessment simply because foreign courts may, by reason of the laws of that foreign country, refuse to recognise the right of deduction so given to the company by the Australian legislature. The majority of the Judges agreed with Dixon, J. In this view as to the scope of the Australian Statute no question of its having extra-territorial effect arises. The Statute was certainly *intra vires*, as the Australian legislature legislated on a subject which was within the territorial limits of Australia. Evatt, J., however, adopted the reasons which he had given in the earlier case, namely in *Trustees, Executors and Agency v. Federal Commissioner of Taxation*¹. In support of his view that the State legislature had power to legislate extra-territorially he gave four reasons:

(i) that the Australian Commonwealth has full self-government and the Commonwealth Parliament has power to legislate extra-territorially, as such a power is an essential part of the conception of self-government;

(ii) that *Croft v. Dunphy*² had laid down that the Canadian Parliament had the powers of a full Sovereign legislature, and the observations made therein would apply to the Commonwealth Parliament of Australia;

(iii) that the legislative powers of the States of the Australian Commonwealth regarding extent are the same as that of the Commonwealth Parliament; and

(iv) that the questioned legislation, even if it had extra-territorial effect, would be perfectly valid, if in some aspects and relations it bears upon the "peace, order and good government" of the Dominion or the constituting States, as the case may be, either generally or in respect to specific subjects.

In my judgment the rules laid down by Evatt, J., in *Trustees, Executors and Agency v. Federal Commissioner of Taxation*¹ cannot be the true guide for deciding the question before us. India is not yet a self-governing unit of the Empire. For all practical purposes it is still a

(1) 49 Commonwealth Reports. 220.

(2) (1933) A.C. 156.

dependency. The Indian Constitution is materially different from Canadian and Australian Constitutions, and Evatt, J., was confining his observations to the constitutions of those two countries, where matters of peace, order and good government were entirely the concern of the Dominion Commonwealth or the States. Besides, his observations do to a certain extent go against the general principle laid down by Lord Halsbury in *MacLeod's case*¹ and is against the decision of Tomlin, J., in *London and South American Investment Trust Limited*¹.

Issue No. 1—The contention of the learned Advocate-General is that the income which has been assessed, *e.g.*, the dividends from the sterling companies did in *fact* arise or accrue to the plaintiff company in British India. If that be so, the plaintiff company would not be affected by Explanation (3) to Section 4 and so would not have the right to question its validity. Moreover, the suit will have to be dismissed on the merits, if his contention be accepted.

For determining this point the material facts are as follows:

- (i) The sterling companies are incorporated in England;
- (ii) The place of central control of those companies is in England;

Their principal place of business is in England. It is from there that their chief operations are controlled, managed and directed;

- (iii) The shares of those companies have been issued in England, the share registers are kept in England, dividends are declared in England and paid in England;

(iv) Those companies carry on business in British India and earn profits here. They have been assessed to income-tax in British India on their profits earned in British India;

- (v) The Raleigh Investment Company is a non-resident Company;

(vi) The dividends in question had been declared and paid to it in England.

Leaving out the case where income is not received in British India, income of a non-resident is assessable in British India only if the income had accrued or had arisen in British India or is deemed to have arisen or accrued in British India. Explanation (3) to Section 4, which deals with dividend only, defines the circumstances under which a class of income actually arising or accruing outside British India is deemed to have arisen or to have accrued in British India. Section 42 which is not relevant to the case before us, for the assessment is not as an agent of the plaintiff company, also mentions the case where income

(1) (1891) L.R. 1891 A.C. 455.

(2) (1927) L.R. 1927, 1 Ch. 107.

would be deemed to have arisen etc., in British India. For the purpose of this issue we have to leave out those two cases, namely Explanation (3) to Section 4 and Section 42. We are to see, fiction apart, whether the income of the company derived from dividends paid by the sterling companies had in fact arisen or accrued in British India. The cases established the following proposition, namely :

“ the *situs* of the income is the *situs* of the fund from which the income is *directly* derived, that is to say, in the case before us, the *situs* of the shares held by the plaintiff company would determine the place where the income had arisen or accrued to it.”

Regarding the *situs* of the shares two views have been maintained namely :

(a) the place of “ residence ” of the company in which the shares are held determining the *situs* of the shares : and

(b) the *situs* of the shares is where the share register of the company is kept.

The main proposition is established by the cases of *Commissioner of Income-tax, Bombay Presidency v. Raja Bahadur Bansilal Motilal*¹, and *Commissioner of Income-tax, Bombay v. Swarup Chand Hukumchand*². This is also the effect of the decision of the Judicial Committee in *Income-tax Commissioner, Bombay v. Chunilal Mehta*³ where the place of profit earning was taken to be the *situs* of the contracts which produced the proof to the assessee.

Regarding *situs* of the shares the first view is what has been adopted in *Bradbury v. English Sewing Cotton Co.*⁴ At page 758, Lord Cave, L.C., observed thus : “ A share or a parcel of stock is an incorporeal thing, carrying the right to a share in the profits of a company ; and where the company is, there the share is also, and there is the source of any dividend paid upon it.” He held that the American Company was resident in England in the three years in question (1914-1915 to 1916-1917), and the dividends received by the English Company by reason of its share holdings in the American Company were income which had accrued to it in England and not from foreign possessions. According to this view the place of residence of the sterling companies in the relevant year would be the determining factor.

The cases on the subject of residence of companies lay down that the place of incorporation of the company is not a very important factor. The accepted view is that for purposes of income-tax a company must be taken to reside at the place from which its real business is carried on, that is to say, “ where the central management and control abides”:

(1) (1930) I.L.R. 54 Bom. 460.

(2) (1931) I.L.R. 55 Bom. 231.

(3) (1938) L.R. 65 I.A. 332 ; 6 L.T.R. 521.

(4) L.R. (1923) A.C. 744.

*De Beers Consolidated Mines Ltd. v. Howe*¹, *Bradbury v. English Sewing Cotton Co.*² A company may no doubt have, like a natural person, more than one place of residence, but in that case the central management and control must be divided and exercised from more places than one: *Swedish Central Ry Co. v. Thompson*³.

The other view is that the *situs* of the shares for purposes of taxing statutes must be taken to be the place where the share register is kept, "for the evidence of title to shares is the share register." This is the view taken in *Brassard v. Smith*⁴, and *London and South American Investment Trust v. British Tobacco Co.*⁵

Whichever view be accepted the *situs* of the shares which the plaintiff company had in the sterling companies would not be in British India but in England. The income in the shape of dividends paid by the sterling companies to the plaintiff company therefore arose or accrued not in British India but in England. The case of the *Commissioner of Income-tax, Bombay v. Major Goldie*⁶ is an authority directly on the point. The plaintiff company has been assessed to income-tax in British India in respect of those dividends on the basis of Explanation (3) to Section 4 of the Indian Income-tax Act, which made, by a fiction so to say, the income from those dividends, which in reality had arisen and accrued outside British India, to be income which had arisen or accrued in British India. The plaintiff company is accordingly entitled to challenge the legality of that explanation.

Issue No. 2.—The second and third issues must be decided on the basis of the allegation that the assessment is *ultra vires*, a point on which I have already recorded my finding. Two grounds have been urged in support of the contention that the provisions of the Income-tax Act bar the suit. It is firstly urged that the *only* manner in which the plaintiff company could proceed to have relief was by following the machinery provided for in the Income-tax Act; by first appealing to the Appellate Assistant Income-tax Commissioner under Section 30, then, to the Appellate Tribunal under Section 33 and then coming up to the High Court by way of reference under Section 66. Secondly, it is contended that Section 67 of the Income-tax Act expressly bars the suit.

The general principle has been formulated by Willes, J., in *Wolverhampton New Water Works Co. v. Hakesworth*⁷. The third proposition that he laid down is that when a statute creates a new liability—a liability not existing at common law—and at the same time

(1) L.R. (1906) A.C. 455.

(2) L.R. (1923) A.C. 744.

(3) L.R. (1925) A.C. 495.

(4) L.R. (1925) A.C. 371.

(5) L.R. (1927) 1 Ch. 107.

(6) (1931) I.L.R. 55 Bom. 734.

(7) 6 C.B.N.S. 236.

gives a special and particular remedy for enforcing it, the remedy provided for in the statute must be followed and the party is not entitled to have recourse to an action in the civil court. In *Bhai Sankar v. The Municipal Commissioners of Bombay*¹, Sir Lawrence Jenkins, C.J., stated the third proposition of Willes, J., in a different form. He thus observed: "But where a special tribunal out of the ordinary course is appointed by an Act to determine questions as to *rights* which are the creation of that Act, then except so far as otherwise expressly provided or necessarily implied, that tribunal's jurisdiction to determine those questions is exclusive." These principles have been applied by the other Indian High Courts and by the Judicial Committee of the Privy Council in *Secretary of State for India v. Mask & Co.*², a case on which the learned Advocate-General has also relied. In my judgment these principles can be invoked by the defendant for the purpose of defeating the suit before us, only if it can be shown that the point raised in the suit and on the basis of which the plaintiff seeks relief, could have been determined by the special tribunals set up by the Income-tax Act.

Section 80 of the Act creates a tribunal to which the assessee dissatisfied with the assessment made by the Income-tax Officer is to go in the first instance. What questions he can raise before that tribunal are indicated in the section itself. He can object to the amount of his income as determined by the Income-tax Officer or to the amount of loss computed under Section 24 or the amount of the tax etc. He can also deny his liability to be assessed *under the Act*. That phrase to my mind means that he can only urge before that tribunal that the provisions *as they stand* in the Act do not make him liable, *i.e.*, exempt his income or a part of his income from assessment. He cannot urge there that though a provision of the Act makes his income or part thereof liable to be assessed, that provision is illegal, being *ultra vires* the Indian Legislature. The Appellate Assistant Commissioner would not be competent to entertain or decide that question. On the principle that the scope of an appeal cannot be enlarged but must be limited to points which were open for adjudication by the court or tribunal of first instance the Appellate Tribunal functioning under the Act, to which an appeal is taken under Section 83, would have no power to entertain the said question and deal with it in its order. This court on a reference being made to it under Section 66 cannot also deal with such a question, as the reference must be limited to points arising out of the order passed by the Appellate Tribunal. I accordingly overrule the first ground of attack made by the defendant.

(1) (1907) I.L.R. 31 Bom. 604.

(2) (1940) L.R. 67 I.A. 222; 3 F.L.J.P.C. 15,

The second ground urged by the learned Advocate-General is that Section 67 of the Act bars the suit. To support their respective contentions the learned Advocates appearing for the parties have cited a large number of decisions. One of the cases on which the learned Advocate-General has most strongly relied is *Secretary of State v. Meyyappu Chettiar*¹. In that case the plaintiff was assessed to income-tax by the Income-tax Officer on a finding that he was a resident of British India. In the suit he alleged that he was not a resident of British India but of Saigon. He prayed for a declaration that the assessment was illegal and for recovery of the money which he had paid on demand by the Income-tax Officer. Section 67 of the Income-tax Act was successfully pleaded and the suit was dismissed. In the course of his judgment Varadachariar, J., observed that where a statute contains a specific provision limiting or excluding the jurisdiction of civil courts the determination of the ambit of the civil courts' jurisdiction must rest upon the language used in the privative provision and cases decided on the provisions of statutes couched in different language would be of little assistance. I agree with those observations to this extent that the language of the privative provision is of prime importance, but I do not agree to the further proposition (if that be its meaning) that it would not be legitimate to refer to decisions given on other statutes even when the privative provisions are of similar scope. I would not, however, burden my judgment by reference to the decision in suits brought for declaration that rates imposed under the provisions of the Bengal Municipal Act had not been legally imposed. I would confine myself to decisions in suits relating to income-tax and to decisions in other suits where the privative provisions in the statute are of similar scope. The first case is *Haji Rehematulla v. Secretary of State for India in Council*². In that case a person, whose place of residence was outside British India, was assessed on profits, which also had accrued outside British India, under the Income-tax Act of 1886 (Act II of 1886). He brought a suit for a declaration that the assessment on him was illegal. Section 39 of Act II of 1886 which is couched exactly in the same terms as the first part of Section 67 was pleaded as a bar to the suit. The plea was overruled on the ground that if the questioned assessment was *ultra vires* that section did not stand in the way of the plaintiff. This case was cited in *Meyyappa Chettiar's case*² but was distinguished on two grounds: (1) that the Act of 1886 contained no provision corresponding to the second part of Section 67, and (2) the said Act did not provide the same safeguards, as in the Act of 1922, by way of appeal and reference to the High Court with a further right of appeal

(1) (1937) I.L.R. 1937 Mad. 211; 4 I.T.R. 341.

(2) (1926) 92 I.C. 351; 2 I.T.C. 118,

to the Privy Council. In my judgment *Haji Rehematulla's case*¹ cannot be put aside on these grounds of distinction. The second part of Section 67 deals with a different subject altogether. The Act of 1886 contained provisions for revision, firstly to the Collector, and then to the Commissioner of the Division. There was no doubt no provision for a reference to the High Court and for further appeal to the Privy Council, but in my judgment the scope of a privative provision like that contained in Section 39 of Act II of 1886 or in the first part of Section 67 of the Act of 1922 would neither be enlarged or curtailed by reason of the number of appeals from the assessment order provided for by the statute. The next case of importance is *Raja of Ramnad v. Secretary of State*². The Income-tax Act under consideration was the Act of 1918. Section 52 contained the privative provision which is exactly in the same terms as Section 67 of the Act of 1922. At page 17 of the report the learned Judges made the following observations: "A civil suit is barred under Section 52 of the Income-tax Act of 1918. If the tax was levied *under that Act*, no doubt, a suit would be barred, but if the assessment was made in respect of an item of income which is not assessable under the Act a civil suit would lie, inasmuch as the officer making the assessment had no jurisdiction to make it. In cases in which the Income-tax Officer has to decide whether a certain item of income is assessable or not, his decision cannot be said to be *ultra vires* even if it is illegal. But where a certain income is *outside the scope of the Act*, such as agricultural income or income not earned in or brought into British India, any assessment in respect of such income would be outside the scope of the Act, and a civil suit to recover it would not be barred by reason of Section 52." In my judgment the rule thus formulated is the correct rule, and further it is on the principle indicated in this passage, that *Meyyappa Chettiar's case*³ and other cases cited by the learned Advocate-General, to which I will refer later on, are to be distinguished. The rule that if the imposition is *ultra vires*, statutory provisions, which purport to take away the jurisdiction of civil courts would not be considered effective to bar a suit receives support from the decision of the Judicial Committee in *Secretary of State v. Fahaminnessa Begum*⁴, where in spite of the provisions of Section 6 of Act IX of 1847 it was held that a civil suit was maintainable to declare that the assessment of revenue made by the revenue authorities was illegal on the ground that on a construction of the provisions of Act IX of 1847 the revenue authorities could not have legally imposed revenue on the land in question. The decision of the Bombay High Court in *Bhag Chand*

(1) (1926) 92 I.C. 351; 2 I.T.C. 118.

(2) (1929) I.L.R. 52 Mad. 12.

(3) (1937) I.L.R. 1937 Mad. 211; 4 I.T.R. 341.

(4) L.R. 17 I.A. 40 at 52.

*Dagdusa v. Secretary of State for India in Council*¹, affirmed on appeal in (54 I.A. 388), on a different ground also supports the same view. In that case a large body of shop-keepers of Malegaon filed a suit against the Secretary of State for India for a declaration that a certain notification issued by the District Magistrate, by which compensation for damage caused at a riot and the costs of additional police for keeping order were to be recovered, was illegal and for injunction. A notice under Section 80 of the Code of Civil Procedure was given, but the suit was filed before the expiry of two months from the date of that notice. The Secretary of State raised three substantial questions: (1) that Section 4 (f) of the Bombay Revenue Jurisdiction Act (Act X of 1876) barred the suit, (2) that the suit having been instituted before two months of the notice given under Section 80 of the Civil Procedure Code was premature, and (3) the challenged notification was a valid one. The trial Court gave effect to all the three contentions and dismissed the suit. On appeal the Judges of the Bombay High Court were divided on the question as to whether notice under Section 80 of the Code of Civil Procedure was required, the suit being for injunction. Both of them held that the notification was perfectly valid, but that if the notification had been illegal the suit would not have been barred under Section 4 (f) of the Bombay Revenue Jurisdiction Act in respect of the tax relating to additional police charges. Shah, A.C.J., observed thus: "Apart from this ground it is clear that the provision (Section 4 (f) of the Revenue Jurisdiction Act) cannot apply where the legality of the order of the Government is questioned. It would apply to a case of rate which is authorised, that is, legally authorised, by the Government. In the present case the legal basis for the action of Government is questioned and I think that the suit is not barred by this clause even as regards the tax relating to additional police charges, provided it is established that the rate is not legal. Thus the objection (about the maintainability of the suit) would apply to police charges, if it be proved that the rate is legally authorised." Section 4 (f) of Act X of 1876 runs as follows: "Subject to the exceptions hereinafter appearing no civil court shall exercise jurisdiction as to any of the following matters :

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(f) claim against the Crown to hold land wholly or partially free from payments charged on or payable out of land revenue, or to set aside any cess or rate authorised by the Government under the provisions of any law for the time being in force."

¹(1) (1927) I.L.R. 48 Bom. 87.

On appeal by the plaintiffs to the Privy Council the suit was dismissed. The Judicial Committee held that the notification so far as it related to the collection of compensation was perfectly valid, but it was not valid so far as it related to the collection of additional police charges. Lord Sumner then went on to examine the position as to whether the suit so far as it related to additional police charges was maintainable or not. He held that it was not maintainable in view of the provisions of Section 80 of the Code of Civil Procedure but at the same time did not dissent from the observations made by the Bombay High Court in respect of the scope of Section 4 (f) of the Revenue Jurisdiction Act.

The cases on which the learned Advocate-General has relied are *Forbes v. Secretary of State for India*¹, *Dr. R. N. Singha v. Secretary of State for India*², *Secretary of State for India v. Forbes*³ and *Secretary of State for India v. Meyyappa Chettiar*⁴. In none of those cases was the question of *ultra vires* raised. In all of them the assessment was not *outside* but *under* the Income-tax Act and the suits challenged the correctness of findings on points which the Income-tax Officer was competent to determine. In *Secretary of State for India v. Mask & Co.*⁵ a case which concerned customs duties, the plaintiff contended that the goods which he had imported were of a different description from what the Customs authorities took them to be and so the proper duty payable was at a lower rate. That case is also of the same type as the first mentioned case. In the suit before us Section 67 is of no avail to the defence as the suit is not for setting aside or modifying an assessment made *under that Act*. It is a suit for a declaration that the assessment is unauthorised by the Act and outside the Act as it ought to stand after Explanation (3) to Section 4 is struck out on the ground that it is *ultra vires* the legislature. I would accordingly answer this issue in favour of the plaintiff.

Issue No. 3—For deciding the third issue the provisions of Section 226 of the Government of India Act, 1935, have to be considered. It is a section which still stands in the statute book in spite of the fact that the historical reasons for the enactment have long disappeared. It has the effect of taking away the original jurisdiction of this Court in matters in respect of which courts subordinate to this Court would have original jurisdiction. It is an anomaly that this Court cannot exercise its functions in the exercise of its original jurisdiction but would be free to do so in the exercise of its appellate jurisdiction in matters concerning revenue. Be that as it may, we have to give effect to that section.

(1) (1915) I.L.R. 42 Cal. 151.

(2) I.L.R. 5 Rang. 825.

(3) (1922) A.I.R. 1922 Pat. 361.

(4) (1937) I.L.R. 1937 Mad. 211; 4 I.T.R. 341.

(5) (1940) L.R. 67 I.A. 222; 3 F.L.J.P.C. 15.

The section is divided into two parts. The Court has no original jurisdiction in (1) any matter concerning revenue or (2) in any matter concerning any act ordered or done in the collection of revenue. I do not agree with the interpretation put upon this section in *The Dewark-hand Cement Co. Ltd. v. Secretary of State for India*¹ to the effect that the two parts of the section express two distinct and mutually exclusive ideas, namely, "the first part refers to *preliminary* proceedings taken for the purpose of determining the amount of revenue and the second part to the machinery to enforce the payment of revenue." The second part no doubt refers to the machinery for enforcing payment of revenue but I am not prepared to say that the first refers *only* to preliminary proceedings taken for the purpose of determining the amount of revenue. Such a view would conflict with the decision of the Judicial Committee in *Alcock, Ashdown & Co. v. Chief Revenue Authority, Bombay*². In that case Lord Phillimore laid down that the High Court in the exercise of its original jurisdiction had power, in spite of Section 106 of the Government of India Act, 1915, to interfere by issuing a prerogative writ at the stage when the preliminary proceedings were being taken for assessing the amount of income-tax. In my judgment the first part of the section includes the matter dealt with in the second part of the section. A matter concerning revenue would include a matter relating to the collection of revenue. In my opinion the second part of the section has been enacted to give an indemnity to revenue officers who in the discharge of their duties may have collected or may have made attempts to collect revenue by passing orders or by doing things which may not be strictly according to law but which they *bona fide* believed to be in accordance with law.

The cases cited by the learned Advocate-General are cases which concerned the collection of what was in fact revenue or was found to be revenue. The first case is the case of *Spooner v. Juddow*³. The act that was done there was an attempt to collect quit rent due to the East India Company by executing a distress warrant. It could not be justified in law, for the distress warrant issued against one person was executed against another and for a liability which was not fully the liability of the latter. A suit for damages was brought against the Government agent who had executed the said warrant. The main defence was that the suit was not maintainable in view of the provisions of Section 9 of 37 Geo. III, c. 142, which was in the same terms as Section 226 of the Government of India Act, 1935. In reversing the judgment of the Bombay Court the Judicial Committee of the Privy

(1) (1939) I.L.R. 1939 Bom. 320; 2 F.L.J.H.C. 60. (2) (1923) L.R. 50 L.A. 227.

(3) (1845-51) 4 M.I.A. 353.

Council pointed out that the case cannot be decided on the plain language of the section, for if the act done was strictly in accordance with law, the section would be redundant. The section was accordingly interpreted in the manner which I have indicated above. The cases of *Messrs. Best & Co. v. The Collector of Madras*¹, *Gobindarajulu Naidu v. Secretary of State for India*², *Thin Yen v. Secretary of State for India*³, *Dewarkhand Cement Co. Ltd. v. Secretary of State for India*⁴, *Thyagaraja Chettiar v. Collector of Madura*⁵ and *Bhimwandiwalla v. Secretary of State for India*⁶ are cases which fall within the second part of Section 226. In all the cases except the last the act ordered or done by the revenue authorities related to collection of what was admittedly and beyond question revenue and in the last mentioned case as also in *Spooner's case*, what was ordered to be collected was found to be revenue by the Court after adjudication. In all those cases the construction given to the second part of the section in *Spooner v. Juddow*⁷ was re-iterated. *Spooner's case*, and *Bhimwandiwalla's case*, are of importance for the purpose of showing that where there is a dispute as to whether a particular levy is revenue or not, that dispute must be adjudicated upon by the court and only if the court finds that it is revenue, then and then only can the bar of Section 226 be invoked and applied. In my judgment that is the correct approach, as it accords with fundamental principles. The first proposition that is well established is that the condition on which the right of a court of limited jurisdiction to exercise jurisdiction depends must be fulfilled. Those conditions may be of various kinds. They may be founded either upon the character of constitution of the tribunal, or upon the nature of the subject matter of enquiry, or upon certain proceedings which have been made essential preliminaries to the enquiry, or upon the existence of some facts. If there is any dispute as to those facts that Court is not only entitled to adjudicate upon them but must do so. Only its decision on the point would be open for re-examination by a superior court or tribunal: *Colonial Bank of Australasia v. Willan*⁸. It follows as a converse proposition that where a court has a general jurisdiction, that is to say, jurisdiction to entertain suits for proceedings of a civil nature, and its jurisdiction over a particular subject matter, which would otherwise be within its competence, is excluded by a statute, and there is a dispute as to facts, which if established, would oust its jurisdiction, that Court would have not only the power but would be under a duty to give its decision on the said dispute, unless

(1) (1918) 35 M.L.J. 23.

(5) (1936) 59 Mad. 702; 4 I.T.R. 56.

(2) (1927) I.L.R. 50 Mad. 449.

(6) (1937) A.I.R. 1937 Mad. 536.

(3) (1939) I.L.R. 1939, 1 Cal. 257; 3 F.L.J.H.C. 50. (7) (1845-51) 4 M.I.A. 353.

(4) (1939) I.L.R. 1939 Bom. 320; 2 F.L.J.H.C. 60. (8) (1874) L.R. 5 P.C. 417; at 422 to 424.

the private statute plainly prohibits it from adjudicating upon those disputed facts. In the light of these principles this court has the power to determine whether the subject matter of this suit concerns revenue. If it does, the suit would be barred, otherwise not. In my judgment the suit would not be barred simply because what has been imposed on the plaintiff company is or can be called revenue in the popular sense or the defendant gives it that designation. Revenue is that which the State collects from the subject or from the possessions of the State for the purpose of carrying out its administrative and governmental duties. In the first mentioned case it involves the *right* to levy from the subjects. If the right does not exist in respect of a particular matter, what is assessed or collected would not in my judgment be considered as revenue within the meaning of Section 226, although the name of a tax may be given to it. Without a valid act on the part of the State, what is called or designated by it as revenue cannot be revenue. In this view of the matter I agree with the concession that was made by the Advocate-General, Bombay, in *Byramjee Jeejeebhoy v. Province of Bombay*¹, that Section 226 of the Government of India Act contemplates a "valid revenue," and with the observation of Beaumont, C.J., that "before the Section (226) can apply, however, we must determine that the tax which is challenged is legal; if it is not, its imposition does not concern revenue." I accordingly hold that Section 226 is not a bar, the questioned tax imposed on the plaintiff company being illegal, as Explanation (3) to Section 4 is *ultra vires* the Indian Legislature.

Issue No. 5.—On the conclusions to which I have arrived at the company is entitled to the relief as prayed for in prayer (b) of the plaint. The company is also entitled to get a refund of Rs. 4,35,290-5-0 which was paid by it. I have already held that Explanation (3) to Section 4 being *ultra vires* the Indian Legislature, that sum cannot be called revenue, and consequently the second part of Section 226 of the Government of India Act, 1935, places no bar. Even before the Income-tax Officer the company had taken up the position that it was not liable to be taxed in British India on dividends paid by the sterling companies. On a demand notice being served requiring payment of the amount by the 15th March, 1941, it pleaded for time by cable but the answer was that time could not be extended and that if the payment was not made by the 15th March, 1941, the company would be treated as in default, which implied that a penalty, which may be equal to the amount of the assessed tax, may be imposed. On these facts I hold that not only the payment was made under protest, but it was made under circumstances which would entitle the company to recover it on the basis of

Section 72 of the Indian Contract Act as interpreted by the Judicial Committee of the Privy Council in *Seth Kanhaya Lal v. The National Bank of India Ltd.*¹ The company would also be entitled to recover interest on the said amount from the date of demand (22nd December 1941) till recovery. I agree with my Lord the Chief Justice that the rate should be 4 per cent. simple.

I do not see my way to grant prayer (c). There is no likelihood that the Income-tax Officer would make any attempt in future to assess the company on dividends from the sterling company, if our judgment to the effect that the assessment is illegal, be upheld on appeal.

LODGE, J.—I am in entire agreement with the opinion expressed by Mitter, J., on issues Nos. 2 and 4 as framed by him and with the reasons given, and I have nothing to add to his judgment so far as these issues are concerned.

In placing his argument on issue No. 1, Sir A. K. Roy enunciated the following propositions :—

The plaintiff Company held shares in the sterling companies, i.e., invested money in the sterling companies. In order to obtain an income, the sterling companies had to do business—the shares would not of themselves earn any income. Therefore the income came through the business operations of the sterling companies carried on in India. The profits of the sterling companies became the subject matter of taxation in British India and were taxed and thereby impressed, as it were, with a label that they were something which had arisen or accrued in British India. The dividends were paid out of those profits. It is normally to be expected that dividends will be declared when profits are made; the profits of the sterling companies constituted the income of the share-holders, though at that stage inchoate. The resolutions of the Boards of Directors declaring dividends did not produce the income: they merely released it. This release was merely the last stage in the process of accrual.

This argument implies that the income of the Company is in fact the income of the share-holders and that the company is merely the channel through which that income is received. It also implies that money received by way of profits in India retains its identity (as though it were a manufactured product stamped "Made in India") as it subsequently passes from hand to hand.

Mitter, J., has shown in his judgment that there is the highest judicial authority for the view that the income of the share-holder is quite distinct from the income of the Company, even when the whole

(1) L.R. 40 I.A. 56.

of the share capital is held by one share-holder. It seems to me that the provisions of the Indian Income-tax Act itself lead to the same conclusion. Under the provisions of that Act a company pays income-tax and super-tax on its profits. Thereafter the share-holder who receives a dividend is assessed to income-tax and super-tax on that dividend. The share-holder is required however to pay income-tax not on the amount of the dividend actually received, but on that amount increased by a proportionate share of the income-tax paid by the company. He is then credited with having paid that proportionate share, as income-tax. When it comes to super-tax however, no credit is given to the share-holder for the super-tax already paid and he is again required to pay super-tax on the dividend so increased. It follows that either the share-holder is assessed twice to super-tax on the same income or the income of the share-holder is, for the purposes of the Indian Income-tax Act, regarded as distinct and separate from the income of the company. As the Indian Income-tax Act does not authorise the assessment of a person twice to super-tax on the same income the second of the above views must be correct.

The second argument that the money received as profits retains its identity when passed on, is in my opinion equally fallacious. If this argument were sound it would follow that the income of employees of the sterling companies, received in the form of salaries in London for work done in London, would have a source or origin in India, and would have to be regarded as accruing or arising in India—a view which seems to me untenable.

For these reasons, and for the reasons given by Mitter, J., in his judgment, I agree that issue No. 1 must be answered in the affirmative.

Issue No. 3.—I am unable to accept the view that Section 226 of the Government of India Act, 1935, is not a bar to our exercising jurisdiction in the matters now before us. That section is a relic of an old quarrel and is founded on considerations essentially different from those on which provisions such as those in Section 67 of the Income-tax Act are based. The jurisdiction of the Civil Courts is excluded by Section 67 of the Income-tax Act and by similar sections in other statutes because under those statutes other tribunals have been established to give the necessary relief to aggrieved parties. But Section 226 of the Government of India Act operates whether the aggrieved person has or has not a remedy under the particular Act. Indeed, the very wording of the section indicates that there may be instances when an aggrieved person will have a remedy in the Civil Courts if the cause of action arises outside the territorial limits of the original jurisdiction of the High Court but will have no such

remedy if the cause of action arises within those limits. For these reasons it seems to me that no assistance to the undertaking of the provisions of this section can be obtained from the reasoning given in decisions as to the applicability of such provisions as Section 67 of the Income-tax Act.

Section 226 (1) of the Government of India Act, 1935, reads as follows:

“Until otherwise provided by Act of the appropriate legislature, no High Court shall have any original jurisdiction in any matter concerning the revenue, or concerning any act ordered or done in the collection thereof according to the usage and practice of the country or the law for the time being in force.”

The plaintiffs contend that if any provision of the Income-tax Act is *ultra vires* of the Indian Legislature the giving of a decision that it is *ultra vires* is not the exercise of original jurisdiction in any matter concerning the revenue, nor does it concern any act ordered or done in the collection thereof according to the law for the time being in force.

Mitter, J., in his judgment has pointed out that none of the rulings in which Section 226 of the Government of India Act, 1935, was held to be a bar, is of any assistance to us, inasmuch as in each of those cases the Court was concerned with “an act ordered or done in the collection of the revenue according to the usage and practice of the country or the law for the time being in force”; and there was no question whether the provisions of the Act were *ultra vires* of the Indian Legislature.

I have no difficulty in accepting the argument that where a provision of the statute is found to be *ultra vires* of the legislature, an act ordered or done under the provision is not an act ordered or done according to the law for the time being in force, and therefore the original jurisdiction of the High Court to determine whether a provision is *ultra vires* or not, is not excluded by the second part of Section 226 (1) of the Government of India Act. The problem is whether that jurisdiction is excluded by the first part of the section, *viz.*, “No High Court shall have any original jurisdiction in any matter concerning the revenue.”

The cases cited, in which this portion of the section has been considered, are three in number. In *Alcock, Ashdown & Company, Limited v. Chief Revenue Authority, Bombay*¹, the question in issue was whether the High Court had power to make an order requiring the Chief Revenue Authority to perform his statutory duty of stating a case and referring it to the High Court under Section 51 of the Indian

(1) (1923) 50 I.A. 227.

Income-tax Act, 1918. The Judicial Committee observed: "In their Lordships' view the order of the High Court to a revenue officer to do his statutory duty would not be the exercise of "original jurisdiction in any matter concerning the revenue," and the latter part of the clause need not be considered, for the proceedings in this case had not to do with the collection of the revenue, but with the preliminary assessment to ascertain what that revenue was."

This decision emphasises the distinction between two parts of Section 226 (1) of the Government of India Act, 1935, and suggests that if the statutory duty in question has to do with the collection of the revenue, and not merely with the preliminary assessment, the power of the High Court to issue a direction to a revenue officer to perform that duty may possibly be excluded by this section.

But so far as the first part of the section is concerned, this decision does not suggest that any special or limited interpretation is to be placed on the words 'any original jurisdiction in any matter concerning the revenue': the decision merely lays down that the issue of an order to a revenue officer to perform his statutory duty of stating a case is not the exercise of original jurisdiction in a matter concerning the revenue.

In *Dayaldas Kushiram v. The Commissioner of Income-tax, Central and Income-tax Officer, Section II (Central)*¹, it was held that an order directing a revenue officer to forbear from doing something which he believes wrongly to be his statutory duty, cannot fall within Section 226 (1) of the Government of India Act. This decision purports to follow *Alcock, Ashdown & Company, Limited v. Chief Revenue Authority, Bombay*², and for our present purposes, does not go further than the earlier authority.

*Sir Byramjee Jeejeebhoy v. The Province of Bombay and Another*³ is the only decision which seems to me to have a direct bearing on the question before us. In that case the question before the court was whether Part VI of the Bombay Finance Act, 1932, as amended in 1939 was *ultra vires* of the local legislature. Sir Jamshedji Kanga for the plaintiff argued (page 62) "Section 226 of the Government of India Act should be strictly construed. It only takes away the original jurisdiction of the High Court in any matter concerning the revenue. Before the section could operate there must exist a valid Act and without a valid Act there can be no revenue. The jurisdiction to determine the validity of the Act is not taken away by Section 226."

(1) (1940) 8 I.T.R. 139; I.L.R. 1940 Bom. 650; 3 F.L.J.H.C. 75.

(2) (1923) L.R. 50 I.A. 227.

(3) (1940) I.L.R. 1940 Bom. 58; 7 I.T.R. 670; 3 F.L.J.H.C. 23.

The Advocate General in reply conceded (page 66) the point. He argued that Section 226 contemplates the existence of valid revenue and stated that he was unaware of a case where the jurisdiction of the Court was barred when the validity of the Act imposing the revenue was in question. In delivering judgment Beaumont, C. J., observed : " Before the section can apply, however, we must determine that the tax which is challenged is legal ; if it is not, its imposition does not concern revenue, but it is a nullity. To refuse jurisdiction to try this question would involve dismissing the case against the plaintiff without hearing him. This point was not seriously contested by the Advocate General." It is clear from the above that the point was not seriously contested. For myself, with great respect to the learned Judges, I am not satisfied that that decision was correct.

What is the position in the present case? The Central Government in an attempt to increase the revenue considers whether it has a right, to tax certain incomes. Believing in good faith that it has the right it obtains the necessary statutory authority from the Indian Legislature. The Income-tax authorities assess the incomes in question, demand payment of the tax, realise the same and appropriate the money to the revenue of the country. The questions in issue are—Has the Indian Legislature the power to tax these incomes? Can the Indian revenue be increased in this manner? Is the amount realised from the plaintiff, which has been claimed as revenue, realised as revenue, and treated as revenue, to continue to be so treated or is it to be deducted from the funds claimed by Government as its revenue and refunded to the plaintiff.

It seems to me that if the ordinary meaning is to attach to the words ' any matter concerning the revenue ' then all these questions are matters concerning the revenue. In other words, a decision that something is not valid revenue concerns the revenue as much as a decision that it is valid revenue.

The argument that Section 226 is a bar only to the exercise of jurisdiction in matters concerning valid revenue seems to me to conflict with the principle laid down in *Spooner v. Juddow*¹. The same argument would apply to cases where the revenue officer misunderstood the valid provisions of the Act and assessed to tax incomes not assessable under the Act—because the amount realised would not be valid revenue.

Similarly if the revenue officer by mere mistake in arithmetic demanded and realised from an assessee more than was legally payable, the illegal excess would not be valid revenue, and according to this argument, the jurisdiction of the High Court to grant relief in

(1) (1845-51) 4 M.I.A. 353.

respect thereof would not be barred. In other words, the jurisdiction of the High Court would be barred under Section 226 of the Government of India Act, 1935, only in those cases where the plaintiff on the merits was not entitled to succeed. In my opinion neither the plain words of the section nor the decision of the Judicial Committee in *Alcock, Ashdown and Company Ltd.*¹, justify such an interpretation.

I am of opinion that Section 226 of the Government of India Act is a bar to our entertaining the present suit, and that the plaint should therefore be returned to the plaintiff for presentation to the proper court.

It only remains for me to add that if I were not convinced that Section 226 of the Government of India Act was a bar to the exercise of jurisdiction by us in this matter, I should agree with the order proposed by my Lord the Chief Justice.

Order accordingly.

[IN THE LAHORE HIGH COURT.]

NIZAM-UD-DIN AMIR-UD-DIN OF LAHORE, *In re*.

DIN MOHAMMAD and SALE, JJ.

May 31, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE AMENDMENT), SEC. 3
—ASSOCIATION OF INDIVIDUALS—CO-HEIRS OF MOHAMMADAN—MANAGING PROPERTY JOINTLY AND DISTRIBUTING INCOME IN ACCORDANCE WITH THEIR RESPECTIVE SHARES—WHETHER ASSESSABLE AS ASSOCIATION OF INDIVIDUALS.

The assessee who were the co-heirs of a Mohammadan inherited after his death under Mohammadan law specific shares of the property left by him. The assessee did not partition the property and the rent deeds stood in their joint names. They had jointly employed a munshi to manage the property and collect the rents and the income after deducting the cost of collection and other expenses was distributed in accordance with their respective shares. In the assessment year 1937-38 the Income-tax authorities assessed the assessee as an association of individuals :

Held, on a reference, that the assessee did not form an association of individuals and they should be separately assessed on their individual shares.

(1) (1923) L.R. 50 I.A. 227.

Cases referred to :—

Commissioner of Income-tax, Burma v. M.A. Baporia and Others (1939) 7 I.T.R. 225 ; 1939 Rang. L.R. 631 ; A.I.R. 1939 Rang. 258.

Dwarakanath Harischandra Pitale and Another, *In re* (1937) 5 I.T.R. 716 ; A.I.R. 1938 Bom. 353.

Haji Ghulam Hussain and others v. Commissioner of Income-tax,, Lahore (1942) 10 I.T.R. 405.

Case stated under Section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Punjab, N.W.F. and Delhi Provinces. (Civil Reference Case No. 9 of 1941).

STATEMENT OF CASE.

"Facts of the Case.—The assesseees are co-heirs of the late M. Karim Bakhsh. After his death each of the heirs became entitled under Mohammedan law to a specific share in the property which he had acquired, but the property has not in fact been divided. The rent deeds stand in their joint names and they have jointly employed a munshi to manage the property and collect the rents. After the deduction of the cost of collection and other expenses the net income is distributed in accordance with their respective shares.

From 1920-21 to 1934-35 they were jointly assessed as an association of individuals or unregistered firm. In 1935-36 the beneficiaries were assessed on their individual shares, but in 1936-37 the Income-tax Officer again held them to be assessable as an association of individuals. His decision was confirmed by the Assistant Commissioner on appeal and the assesseees did not pursue the matter further.

In connection with their assessment for the year 1937-38, which is the subject of this reference, a return was filed by M. Nizam Din in which he declared an income of only Rs. 3,058, which represented his own 90/288ths share. The shares of the other heirs were separately stated. The Income-tax Officer, however, decided that the co-heirs should continue to be treated as an association of individuals and he made a joint assessment accordingly on a total income of Rs. 10,398. His decision was again confirmed by the Assistant Commissioner. Copies of the assessment and appellate orders are appended as Exhibits 'A' and 'B.' The assesseees then submitted an application under Section 66 (2) but my predecessor held that there were no grounds for a reference. A copy of his order is appended as exhibit 'C.'

Question for consideration.—As a result of a subsequent petition under Section 66 (3) I have now been required to refer the following question :—

"Whether on the facts found in this case it can be held by the Income-tax authorities that an association of individuals exists which can be assessed as an entity or whether the correct finding should be

that there are co-owners with a common manager of property who should be separately assessed on their individual shares?"

Opinion of the Commissioner.—Although each of the heirs is entitled to a definite share they must in my opinion be regarded as having formed themselves into an association of individuals, within the meaning of Section 3 of the Act, when they elected not to divide the property but to retain it in their joint ownership and to manage it as a joint venture producing income. It follows that in my opinion the association is the owner of the property for the purpose of Section 9. I am supported in this opinion by the decisions reported at 5 I.T.R. 716. and 7 I.T.R. 225. The point is no longer of much practical importance since the Income-tax (Amendment) Act, 1939, has added a new sub-section (3) to Section 9 which states that "where property is owned by two or more persons and their respective shares are definite and ascertainable, such persons shall not in respect of such property be assessed as an association of persons, but the share of each such person in the income from the property as computed in accordance with this section shall be included in his total income." In view of this provision the heirs are now being separately assessed on their respective shares. The new sub-section, however, is not applicable to this assessment, and the fact that the Legislature considered it necessary to introduce such a provision seems to me to support the view that associations of this type were previously liable to joint assessment. I submit, therefore, that the first of the alternatives which have been stated in the question should be held to be correct."

Kirpa Ram Bajaj, for the Assessee.

Raj Krishna, for the Commissioner.

ORDER.

This is a case stated by the learned Income-tax Commissioner on a mandamus issued by this Court in which the following question was propounded:—

"Whether on the facts found in this case it can be held by the Income-tax authorities that an association of individuals exists which can be assessed as an entity (by which is obviously meant a unit) or whether the correct finding should be that there are co-owners with a common manager of the property who should be separately assessed on their individual shares?"

The reference related to the assessment for the year 1937-38.

The material facts as found by the learned Commissioner are that the assesseees are co-heirs of the late M. Karim Bakhsh from whom they inherited under Mohammadan Law specific shares of the property left

by him. The income of this property is derived from rent deeds which stand in their joint names. A *munshi* has been employed to manage the property and collect the rent. After the deduction of the cost of collection and other expenses the net income is distributed in accordance with their respective shares.

From 1920-21 to 1934-35 the assesseees were jointly assessed as an association of individuals or unregistered firm. In 1935-36, however, they were assessed on their individual shares. Subsequently, when for the year 1937-38, the Income-tax authorities declined to assess on separate shares but held them assessable as an association of individuals the matter was taken up to the High Court on an application under Section 66 (2) of the Income-tax Act.

On the law as amended with effect from 1-4-39 by the addition of sub-section (8) to Section 9, of the Income-tax Act there can be no doubt that, as admitted by the Income-tax Commissioner, the assesseees must be separately assessed on their respective shares. But the Income-tax Commissioner is of opinion that this amendment altered the law, and that under the law applicable to the assessment of 1937-38, the assesseees must be regarded as having formed themselves into an association of individuals, within the meaning of Section 3 of the Act by reason of the fact that they had not partitioned the property, but retained it in joint ownership and he drew the inference that it was a "joint venture producing income." The learned Income-tax Commissioner referred to *Dwarakanath Harischandra Pitale and Another, In re*¹, and *Commissioner of Income-tax, Burma v. M.A. Baporia and Others*², a Full Bench decision of the Rangoon High Court. Mr. Raj Krishna on behalf of the Income-tax Commissioner has also referred us to a Peshawar case, *Haji Ghulam Hussain and Others v. Commissioner of Income-tax, Lahore*³.

All these authorities agree on one point, *viz.*, that each case must be decided on its own peculiar facts.

The Bombay judgment *Dwarakanath Harischandra Pitale and Another, In re*¹, was a reference relating to Hindu assesseees, and the learned Chief Justice pointed out that the assesseees in the first instance did not constitute an association of individuals. But he held that as soon as they elected to retain the property and manage it "as a joint venture producing income" they became an association of individuals within the meaning of Section 9 of the Income-tax Act. It is doubtful whether this authority can have any application to the facts of the present

(1) (1937) 5 A.I.R. 716.

(2) (1939) 7 I.T.R. 225.

(3) (1942) 10 I.T.R. 405.

case where we are dealing with co-heirs under Mohammadan Law, and when there is no evidence of a "joint venture."

The Rangoon Full Bench decision, *Commissioner of Income-tax, Burma v. M. A. Baporia and Others*¹, is more closely allied to the present case since it was concerned with Mohammadans who inherited shares under their personal law, but the Bench were obviously influenced by the findings of fact which the Income-tax Commissioner had arrived at in that particular case, and it was decided that on the facts therein found there was sufficient material for assessment as an association of individuals. The learned Chief Justice, however, pointed out that "By merely inheriting a share of property, I am satisfied that no person can become a member of an association of individuals unless there is some forbearance or act upon his part to show that his intention and will accompanied the new status."

The Peshawar case, *Haji Ghulam Hussain and Others v. Commissioner of Income-tax, Lahore*², also related to Mohammadans but there again the Bench considered that on the material found by the Commissioner of Income-tax the evidence "though slight, was sufficient for the Income-tax authorities to find that the assesseees were an association of individuals." The fact which mainly influenced the learned Judges was that it was a business concern under which rents were realised jointly and were credited in a joint account in the books.

Here there is no question of the assesseees forming a business concern; and although a *munshi* was employed to collect rents, it has been specifically found that the net income is distributed in accordance with the respective shares of the assesseees, and it would seem, therefore, that there was no joint venture such as was found in the Bombay and Rangoon cases. The mere fact that the assesseees after inheriting their shares of Karim Bakhsh's property, did not choose to partition does not indicate, in my view, that the co-heirs have formed any such combination for the promotion of a joint enterprise or for mutual profit such as is implied in the expression "association of individuals" as used in Section 3 of the Income-tax Act as it stood at the material time. It is pointed out by the learned Chief Justice in *Commissioner of Income-tax, Burma v. M. A. Baporia and Others*³ that the expression "association of individuals" as used in that section must be construed according to the rule of *ejusdem generis* with all the other groups of persons mentioned therein, namely, Hindu undivided family, company and firm; and by merely inheriting shares in a family property, the co-sharers cannot become members of an association of individuals as thus interpreted.

(1) (1939) 7 I.T.R. 225 at p. 237. (2) (1942) 10 I.T.R. 405. (3) (1939) 7 I.T.R. 225 at p. 236.

I would, therefore, answer the reference by saying that for the year 1937-38, the assessees did not form an association of individuals, but should be separately assessed on their individual shares. The petitioners are entitled to the costs of this reference.

DIN MOHAMMAD, J.—I agree. [*Reference answered accordingly.*]

[IN THE LAHORE HIGH COURT.]

SARDARNI NARAIN KAUR AND OTHERS, *In re.*

DIN MOHAMMAD and SALE, JJ.

May 13, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922 AS AMENDED IN 1937), SEC. 16 (3)—TRANSFER OF ASSETS—ASSETS TRANSFERRED TO WIFE BY HUSBAND PRIOR TO 1937 IN ORDER TO SAFEGUARD HER INTEREST—INCOME FROM ASSETS—WHETHER CAN BE INCLUDED IN TOTAL INCOME OF HUSBAND.

The assessee made a gift of certain properties and cash to his second wife several years prior to 1937 in order to safeguard her interest. In assessing the assessee for the year 1937-38, the Income-tax authorities included in the total income of the assessee two items of income representing income from assets transferred to the assessee's wife, under the provisions of Section 16 (3) of the Income-tax Act as amended by the Income-tax (Amendment) Act, 1937:

Held, that Section 16 (3) is applicable to income received from assets which were transferred before the Income-tax (Amendment) Act, 1937, came into force and that as there was no "adequate consideration" for the transfer, the Income-tax authorities rightly included the income received by the wife in the total income of the assessee.

H. P. Banerjee v. Commissioner of Income-tax Bihar & Orissa [1941] (I.L.R. 1941 Pat. 202; 9 I.T.R. 137) and Pandit Gaya Prasad Tewari v. Commissioner of Income-tax, C.P. & U.P. [1942] (10 I.T.R. 308) followed.

Cases referred to:

H. P. Banerjee v. Commissioner of Income-tax, Bihar & Orissa (1941) I.L.R. 1941 Pat. 202; 9 I.T.R. 137.

Pandit Gaya Prasad Tewari v. Commissioner of Income-tax, C.P. & U.P. (1942) 10 I.T.R. 308.

Case stated under Section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Punjab: (Civil Reference No. 7 of 1941).

STATEMENT OF CASE.

Facts of the Case.—For the year 1937-38 Sardar Dayal Singh Man returned an income of Rs. 9,356, but was actually assessed on

Rs. 13,268. The difference is mainly due to the inclusion of two items of Rs. 1,542 and Rs. 1,570, respectively, representing the income from property and bank deposits standing in the name of his wife Sardarni Narain Kaur. In previous years this income had been separately assessed in her hands, but the Income-tax (Amendment) Act, 1937, introduced a new sub-section (now Section 16 (3) of the Indian Income-tax Act) which states that "in computing the total income of any individual for the purpose of assessment, there shall be included so much of the income of a wife or minor child of such individual as arises directly or indirectly.....from assets transferred directly or indirectly to the wife by the husband otherwise than for adequate consideration or in connection with an agreement to live apart." In view of this new provision the Income-tax Officer held that the income in question was assessable in the hands of Sardar Dayal Singh Man, and his decision was confirmed by the Assistant Commissioner on appeal. Copies of the assessment and appellate orders are appended as exhibits 'A' and 'B'. The assessee then submitted an application under Section 66 (2). My predecessor first remanded the case to the Income-tax Officer for further enquiries regarding the source of the assets from which the income was derived. In his report (Exhibit 'C') the Income-tax Officer stated that he was satisfied from the evidence recorded before him that the property and the bank deposits represented assets transferred by Sardar Dayal Singh Man to his wife. He further stated that no adequate consideration for the transfers has been established. In view of this report my predecessor refused to interfere with the assessment and rejected the application for a reference to the High Court. A copy of his order is appended as Exhibit 'D'.

Question for consideration.—The executors of the estate of Sardar Dayal Singh (who has died since the assessment was made) submitted a petition to the High Court under Section 66 (3), and I have now been required to refer the following question:—

"Whether the inclusion in the income of the assessee of the sum of Rs. 1,542 which Sardarni Narain Kaur has received on account of rent accruing from the immovable property standing in her name, and of the sum of Rs. 1,570 which she has received on account of interest on the deposits standing in her name in the Banks is legally justified?"

Opinion of the Commissioner.—As I have already indicated there was some dispute at the earlier stages of the proceedings with regard to the actual origin of the assets from which the income is derived. The assessment order for 1934-35 contains the following statement on the subject:—

"The assessee explains that since his present wife is the second wife and since she had no issue of her own, he gifted away to her the properties as well as the cash money many years ago. This was done in order to safeguard her interest, as the assessee has children from his first wife who would have otherwise inherited the whole of the property."

The assessee subsequently denied having made such a statement, but in the course of the enquiries made by the Income-tax Officer in connection with the present assessment Sardarni Narain Kaur admitted that the nucleus of her property came from gifts made by her husband from time to time, and in the application filed under Section 66 (3) it has been contended, *inter alia*, "that a *bona fide* actual gift of properties by a husband to a second wife in order to safeguard her interests and to make her independent of children from the first wife (legal heirs), as admittedly done in this case, was 'adequate consideration' for the purposes of Section 16 (3) (iii)." The words which I have underlined seem to settle the matter.

Since it is now admitted that the assets were derived from the husband the only questions which remain to be considered are whether Section 16 (3) is applicable to income received from assets which were transferred before the Income-tax (Amendment) Act, 1937, came into force, and whether there was adequate consideration for the transfers made in the present case. In this connection I do not think I need do more than refer to the orders passed by a Full Bench of the Patna High Court on the 20th of November, 1940, in the case of *Rai Bahadur H. P. Banerjee v. Commissioner of Income-tax, Bihar and Orissa*¹, where it has been held that the new sub-section is applicable to income derived from earlier transfers and that "love and affection" cannot be regarded as "adequate consideration". I am respectfully in agreement with these conclusions and I consider that they are clearly applicable to the present case. The assessee has not used the words "love and affection," but it has been stated that the transfers were made in order to safeguard the interests of the second wife, and there is no evidence that any consideration other than love and affection was received.

I submit, therefore, that the question should be answered in the affirmative."

Durga Dass, for the assessee.

Raj Krishna, for the Commissioner.

JUDGMENT.

This is a case stated by the Commissioner of Income-tax under Section 66 (3) of the Indian Income-tax Act, 1922. The mandamus in (1) (1941) 9 I.T.R. 137,

this case was issued on 29th November 1940 and the following question was formulated :—

“ Whether the inclusion in the income of the assessee of the sum of Rs. 1,542 which Sardarni Narain Kaur has received on account of rent accruing from the immovable property standing in her name, and of the sum of Rs. 1,570 which she has received on account of interest on the deposits standing in her name in the Banks is legally justified ? ”

The circumstances which necessitated the propounding of this question were these. A vacant site situate at Rawalpindi was purchased in the name of Sardarni Narain Kaur, wife of Sardar Dayal Singh Man as long ago as October 1912 and later a residential house was constructed thereon. Two houses situated at Murree were subsequently purchased in the name of the same lady on the 13th July 1919 and on the 16th July 1919 respectively. Besides, some cash had been deposited in the Banks by the lady in her own name by way of fixed deposit. Upto the assessment year 1936-37 the income derived from the properties mentioned above was assessed in the hands of the lady herself. Then came the Indian Income-tax (Amendment) Act, 1937, (IV of 1937) which introduced a new sub-section in Section 16. By that sub-section it was enacted *inter alia* that in computing the total income of any individual for the purpose of assessment, so much of the income of a wife shall be included which arose directly or indirectly from assets transferred directly or indirectly to the wife by the husband otherwise than for adequate consideration or in connection with an agreement to live apart. In the year 1937-38, therefore when a return was made by Sardar Dayal Singh Man, the two sums mentioned in the question under reference were included in his return as assessable income; the lady having stated that the nucleus of her property started from the gifts made by Sardar Dayal Singh Man to her from time to time. An appeal against that order was taken to the Court of the Assistant Commissioner, but he agreed with the Income-tax Officer that the case was fully covered by the substantive part of Section 16 (3) (iii). The Commissioner was then moved under Section 66 (2), but to no avail. Against the order of the Commissioner this Court granted the mandamus as stated above. It may be remarked that Sardar Dayal Singh Man died during the course of this assessment and his estate is represented by his executors who along with the lady are at present interested in the matter.

The Commissioner in the case stated by him has once more expressed an opinion that there being no adequate consideration for the gifts alleged to have been made in favour of Sardarni Narain Kaur, the income

derived by her from the property standing in her name could not but be computed as the income of her deceased husband, Sardar Dayal Singh Man. Counsel for the petitioners, however, challenges this proposition on the grounds :—

(1) that Section 16 (3) (iii) contemplates bogus transfers only and does not hit genuine transfers made by husbands in favour of their wives ;

(2) that consideration as contemplated in that provision of law is to be interpreted in its dictionary sense and not in its legal sense ;

(3) that this provision of law, if interpreted on the lines indicated by the Commissioner, would involve an interference with the statutory right of transfers vested in the subject under his personal law ; and

(4) that at any rate the provision can have no retrospective effect so as to apply to incomes derived from those transfers which had been effected prior to the amending Act.

In my view, none of these contentions can prevail. It cannot in any circumstance be argued that Section 16 (3) as worded was intended to cover those transactions only which could be characterised as sham or bogus. In fact, a perusal of the various clauses and sub-clauses included in that sub-section clearly points to the contrary. For example, sub-section (3) (a) (i) deals with the income of the wife from her membership in a firm of which her husband is a partner ; (3) (a) (ii) contemplates income derived by a minor who is admitted to the benefits of partnership in a firm of which his father is a partner ; and (3) (a) (iv) mentions the income accruing to a minor child, not being a married daughter, from assets transferred to him by the assessee. In none of these sub-clauses there is even a remote reference to any of these transfers being fictitious. It cannot, therefore, be reasonably urged that in sub-section (3) (a) (iii) only was a transfer of a fraudulent nature alone under contemplation. It is a well established canon of the interpretation of statutes that nothing should be subtracted from or added to an enactment unless the context permits it, and there is nothing in this section which justifies the limited interpretation suggested on behalf of the petitioners.

Similarly the term 'consideration' as used in this sub-clause cannot be said to have been used in its ordinary sense of 'motive' or 'reason' but in its legal signification only. It is contended on behalf of the petitioners that the meaning assigned to the term 'consideration' in the Contract Act cannot in any circumstances be assigned to the term as used in the Indian Income-tax Act inasmuch as by Section 2 of

the Contract Act itself those meanings are confined to that Act alone. No doubt this is so, but this does not justify the further conclusion that the very same term as used in the Indian Income-tax Act should carry a different meaning altogether. I am supported in this view by the use of the term "adequate" before the term "consideration". The term "adequate consideration" is a legal term and must carry the meaning which is ordinarily assigned to it. Moreover, the alternative case dealt with in this sub-clause itself, in my view, clinches the whole matter. The transfer should either be for adequate consideration or in connection with an agreement to live apart and such agreements obviously involve a monetary consideration and not a mere sentimental consideration. That there can be such transfers is evident. Take for example a *hiba-bil-iwaz* contemplated by Mohammadan Law or a transfer in discharge of one's dower debt. If the term 'consideration' would be taken to mean 'reason' or 'motive' only, transfers made by husbands in favour of their wives for monetary consideration would be excluded from the benefit of the exception provided in this sub-clause, and this would make the provision simply absurd.

Similarly, there is no force in the objection raised on behalf of the petitioners that if effect is given to the interpretation put upon this sub-section by the Commissioner, it would involve a direct interference with the right of the subject to make any transfer in favour of his wife or child as he chooses. No such interference is contemplated nor are such transfers invalidated in any manner by this sub-section. All that is laid down there is that the income derived by the transferees from the properties so transferred would be computed as the income of the transferor and this in no way implies that those transfers themselves are in any way invalid. On the other hand, the validity of such transfers is assumed in the provision itself and it is only on that basis that proper effect can be given to this legislative enactment.

The last objection is equally devoid of force. By Section 5 of the amending Act (IV of 1937) it was stated that the amendment made shall not have effect in respect of any income chargeable to income-tax for any year ending before the 1st day of April 1937 and this evidently connotes that any income accruing from the properties contemplated in the new sub-section added to Section 16 after the material date would be assessed in the manner laid down therein. The date of the transfer contemplated in that sub-section, therefore, is altogether immaterial. If income accruing after the date when the Act came into force are only affected by the amendment, by no stretch of language can it be argued that in assessing the income on previous transfers the amendment is given a retrospective effect.

The questions now raised before us have been fully discussed by a Full Bench of the Patna High Court in *H. P. Banerjee v. Commissioner of Income-tax, Bihar & Orissa*¹ which was followed by a special Bench of the Allahabad High Court in *Pandit Gaya Prasad Tewari v. Commissioner of Income-tax, C.P. & U.P.*², and if I may say so with all respect, I am in full agreement with the views expressed therein. I would accordingly answer the question in the affirmative and allow full costs to the Commissioner in this Court.

SALE, J.—I agree.

Reference answered in the affirmative.

[IN THE MADRAS HIGH COURT].

MASK AND CO. v. COMMISSIONER OF INCOME-TAX, MADRAS.

SIR LIONEL LEACH, C. J., and LAKSEMANA RAO, J.

July 30, 1943.

INDIAN INCOME-TAX ACT (XI of 1922), SEC. 10 (2) (xii)—BUSINESS EXPENDITURE—AGREEMENT BETWEEN BUSINESSMEN OF SAME LINE TO SELL AT PARTICULAR RATES—DISHONEST BREACH OF AGREEMENT—SUM PAID AS DAMAGES AND COSTS—WHETHER ALLOWABLE DEDUCTION.

The assessee, a firm carrying on business in crackers, entered into a contract with other traders in the same line of business, under which the assessee's goods were to be sold at certain specified rates, but in breach of this contract the assessee sold crackers at lower rates. In a suit for damages for breach of contract instituted by the other parties a decree was passed against the assessee for Rs. 5,000 and costs. The assessee claimed that the amount paid by the assessee under the decree should be allowed as business expenditure in computing the profits of his business :

Held, that the assessee's action in disregarding the undertaking given was palpably dishonest and the award of damages which followed was not incidental to the trade and did not constitute an expenditure falling within Section 10 (2) (xii) of the Indian Income-tax Act.

Inland Revenue Commissioners v. Von Glehn & Co. ([1920] 2 K. B. 553) and *Inland Revenue Commissioners v. Warnes & Co.* ([1919] 2 K.B. 444) distinguished. :

(1) (1941) I.L.R. 1941 Pat. 202 ; 9 I.T.R. 137.

(2) (1942) 10 I.T.R. 308.

Cases referred to :

Inland Revenue Commissioners v. Warnes and Co. ([1919] 2 K.B. 444; 12 Tax Cas. 227; 89 L.J.K.B. 6; 121 L.T. 125; 35 T.L.R. 436).

Inland Revenue Commissioners v. Vohn Glehn & Co. ([1920] 2 K.B. 553; 89 L.J.K.B. 590; 123 L.T. 338; 35 T.L.R. 436; 12 Tax Cas. 232).

Case referred to the Madras High Court by the Income-tax Appellate Tribunal, Calcutta Bench, under Section 66 (1) of the Income-tax Act XI of 1922 as amended by Section 92 of the Income-tax (Amendment) Act VII of 1939 in Application No. 66 R.A. No. 12 Madras of 1942-43 (Assessment year 1940-41) on its file for decision on the following question of law *viz.*

“ Whether the sum of Rs. 6,203 being costs and damages incurred in connection with an action for breach of contract is not expenditure laid out or expended wholly and exclusively for purpose of the assessee's business within the meaning of Section 10 (2) (xii) of the Act ? ”

Case Referred No. 6 of 1943.

Under Section 33 of the Indian Income-tax Act (XI of 1922) the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. VERMA (Judicial Member) and P. N. S. AIYAR (Accountant Member) delivered the following judgment on 10th August 1942.

JUDGMENT OF APPELLATE TRIBUNAL.

“ This is an appeal preferred by the Income-tax Officer, Cuddalore, praying that the amount of Rs. 6,203 allowed by the Appellate Assistant Commissioner as business expense to the respondent may be disallowed. The question arose in the following circumstances:—

2. The respondent was assessed on an income of Rs. 28,971 from various sources and a sum of Rs. 6,203 was claimed by the respondent on account of court costs and damages which he had to pay to one Salai Mohammad Haji Ibrahim Sait. The respondent and three others had entered into an agreement in 1938 in connection with business in crackers to sell several kinds of cracker at the rates given in the Schedule thereto. The respondent did not abide by the terms of this agreement and sold his crackers at *rates lower than those* given in the schedule, whereupon Salai Mohammad Haji Ibrahim Sait filed a suit for damages of Rs. 5,000 against the respondent. The High Court of Judicature at Madras on its original side in suit C. S. No. 146/34 awarded damages of Rs. 5,000 as well as the court costs to the plaintiff in that case. The respondent paid the damages and incurred expenses for defending the suits amounting to Rs. 1,203. The respondent claimed this sum of Rs. 6,203 as a business expense, which the Appellate Assistant Commissioner had allowed.

3. The Income-tax Officer, the appellant in this case, disallowed this alleged expense on the ground that the damages paid for breach of contract and the court expenses incurred by him in connection therewith could not be regarded as expenditure laid out or expended wholly and exclusively for the purposes of the assessee's business within the meaning of Section 10 (2) (xii) of the Indian Income-tax Act.

4. The Appellate Assistant Commissioner, whose order is under appeal, came to the conclusion that the respondent undersold the goods so that he might steal a march over his competitors. His object in doing so could have been nothing else than, the Appellate Assistant Commissioner proceeded, that to augment his profits and he must necessarily have augmented his profits. The profits earned were more than Rs. 5,000 according to the Appellate Assistant Commissioner and he thought that the breach of agreement was purposely committed for purposes of earning the profits. Relying on the authority of the case reported in *Strong & Co. Ltd. v. Woodifield*¹ the Appellate Assistant Commissioner held that, the test laid down by Lord Davey in the words: "In my opinion, it does not follow that if a loss is in any sense connected with the trade, it must always be allowed as a deduction; for it may be only remotely connected with the trade or it may be connected with something else quite as much as or even more than with the trade. I think only such losses can be deducted as are connected with the trade in the sense that they are really incidental to the trade itself.....It is not enough that the disbursement is made in the course of, or arises out of, or is connected with the trade, or is made out of the profits of the trade. It must be made for the purpose of earning the profits" was satisfied. The only relevant section under which the expenses could be allowed is Section 10 (2) (xii) of the Income-tax Act which is as under:—

"Such profits or gains shall be computed after making the following allowance, namely, any expenditure not being in the nature of capital expenditure or personal expenses of the assessee laid out or expended wholly and exclusively for the purpose of such business, profession or vocation".

The purpose, therefore, must be a purpose connected with business, profession or vocation. All expenses cannot be said to be for trade or business. The basis of the allowance of the claim by the Appellate Assistant Commissioner is that the respondent has made profits on account of under-selling and that it was premeditated. It is not possible to say whether the respondent did make any more profits by under-selling than if he had kept to the terms of the agreement.

5. It is contended for the Income-tax Officer that the expenses must be in the nature of or incidental to the business and not in the nature of damages which may have to be paid for breach of contract. Certain damages arising in the course of business are certainly allowable but the payment of this nature for compensating the other competitors for the loss they have suffered is not an expense laid out for the purpose of business.

6. We are referred to the pleadings in the case and the orders passed by the learned Judges of the Madras High Court on appeal in the case C. S. No. 146/34 referred to above. The words "for purposes of trade" should mean "for purposes of earning profits in trade." The damages which have been awarded against the respondent are not in the nature of any expenses allowable and did not arise in the ordinary course of business itself. It has been extraneous to the business in committing the breach of agreement in the manner of carrying on of the business. The question whether this money has been spent wholly and exclusively for purposes of trade is to be decided, because one has to attend to the true nature of the expenditure and to ask oneself the question, is it a part of the respondent's working expenses? Is it an expenditure laid out as part of the process of profit-earning or, on the other hand, is it any other? The Appellate Assistant Commissioner relied on the observation of Lord Davey in the case of *Strong & Co., Ltd. v. Woodifield*¹, quoted above. This ruling itself indicates that the expenses should be for purposes of carrying on the business and earning profits in the trade. What is found is that this payment of Rs. 6,208 is made not because the respondent has made a profit, but it has no relation either immediate or remote with the profit made or could be made by him. It was awarded because he caused wrongful loss to another. Payments for such acts cannot be said to be laid out for the purposes of business carried on by the respondent. In the same case as relied on by the Appellate Assistant Commissioner (5 I.T.C. 215) it has been laid down :—

"The payment of these damages was not money expended for the purpose of the trade. It is not enough that the disbursement is made in the course of, or arises out of, or is connected, with the trade. It must be made for the purpose of earning the profits."

The ruling laid down in the case of *Commissioners of Inland Revenue v. Alexander Von Glehn & Co., Ltd.*² is also pertinent to the case before us. It has been held that the penalty and costs which a company had to pay for exporting goods to Russia and Scandinavia in violation of the Customs (War Powers) Act, 1915, were not admissible

(1) (1906) 5 Tax Cas. 215.

(2) (1920) 12 Tax Cas. 232.

deductions in arriving at the profits of the company's trade for Excess Profits Duty purposes.

7. In another case reported in *Secretary, Board of Revenue, Income-tax, Madras v. B. Muniswami Chetty & Sons*¹, it has been held :—

“that the assessee was not entitled in arriving at the taxable profits to deduct expenditure incurred by him (a) in employing accountants and lawyers in connection with a dispute between them and the Government as to the amount of excess profits duty payable for the previous year, and (b) similar expenses incurred in arriving at the income on which assessment to income-tax was made or was to be made.

These charges were not expended for the sole purpose of earning profits within the meaning of Section 9 (2) (xi) of the Indian Income-tax Act and hence were not permissible deductions thereunder.”

The expenses claimed as damages in this case, therefore, have really nothing to do with the trade itself.

8. We think, there is much force in the appeal of the Income-tax Officer and disagreeing with the Appellate Assistant Commissioner, we restore the order of the Income-tax Officer disallowing Rs. 6,203 as a business expense.

9. The result is that the appeal is allowed.”

On the application of the assessee under Section 66 (1) of the Indian Income-tax Act (XI of 1922) the Appellate Tribunal referred the case to the Madras High Court.

STATEMENT OF CASE.

“The applicant seeks to refer to the High Court at Madras the following question of law arising in the circumstances which follow :—

“Whether the costs and damages sustained were not incidental to the business of the applicant and whether it is not in the nature of a trading or commercial loss and whether it is not allowable under Section 10 (2) (xii) of the Indian Income-tax Act.”

2. The Commissioner of Income-tax, Madras, who is the respondent to the petition for reference stated in his reply under Rule 54 of the Tribunal Rules that the only question of law which arises is as follows :—

“Whether the sum of Rs. 6,203 being costs and damages incurred in connection with an action for breach of contract is not expenditure laid out or expended wholly and exclusively for purposes of the assessee's business within the meaning of Section 10 (2) (xii) of the Act.”

(1) (1923) 1 I.T.C. 227.

We have heard the arguments of the parties and have come to the conclusion that this application for reference raises a question of law and we proceed to state the case for reference to the High Court of Judicature at Madras.

3. *Statement of the Case.*—The applicant entered into an agreement with certain other fellow-traders in connection with business in crackers to sell several kinds of cracker at certain specified rates. The applicant broke this contract with his fellow-traders and sold his crackers at rates lower than those agreed to between the parties. A suit was filed in the High Court at Madras on its original side by his competitors, parties to the agreement for sale of the crackers at the specified rates, and in the said suit the High Court awarded damages of Rs. 5,000 as well as the court costs to the plaintiffs in that case. Thus a total sum of Rs. 6,203 was claimed before the Income-tax Officer as the expenses incurred for the sake of earning the profits. The Income-tax Officer disallowed this sum. But on appeal to the Appellate Assistant Commissioner, this sum was allowed as a business expense. The Income-tax Officer thereupon preferred an appeal before us which he was entitled to. We came to the conclusion for reasons recorded in our order, dated the 10th August 1942 in appeal R.A.A. No. 128—Madras of 1941-42 that the Income-tax Officer was right in disallowing Rs. 6,203 as damages and the appeal was consequently allowed. The result was that the sum of Rs. 6,203 claimed by the applicant as damages and court costs for breach of contract was disallowed. The question of law which the applicant seeks to refer to the High Court is whether these damages and court costs are an allowable deduction under Section 10 (2) (xii) of the Indian Income-tax Act. It is submitted before us in the petition that the expenses incurred by the applicant were in the applicant's capacity or character of a trader, and not in any other character and not unconnected with his business and that the acts complained of amounted to only a negligent way of carrying on business which causes a contemplable commercial loss, and that this did in fact lead to the sale of their stock of goods, and that damages for breach was part of and incidental to trade. Ordinarily the question whether the expense has been incurred in connection with his business or not would be a question of fact and no reference would lie. But considering that the point in consideration is inter-mixed with a legal question in determining as to what is or is not a business expense and considering that certain cases and decisions of the High Courts were considered by this Bench of the Tribunal in arriving at the conclusion, we think that a reference lies.

4. The question of law therefore which is submitted to the High Court under Section 66 of the Income-tax Act for reference may be stated as under :—

Question of law referred :—“ Whether the sum of Rs. 6,203 being costs and damages incurred in connection with an action for breach of contract is not expenditure laid out or expended wholly and exclusively for purposes of the assessee's business within the meaning of Section 10 (2) (xii) of the Act ? ”

5. The papers mentioned in the index attached will form the paper book in this case.”

M. Subbaraya Ayyar, for the assessee.

K. V. Sesa Ayyangar, for the Commissioner.

JUDGMENT.

(Judgment of the Court was delivered by the Honourable the Chief Justice).

The assessee in this case is a firm carrying on business in crackers. The assessee entered into a contract with other traders in the same line of business, under which the firm's goods were to be sold at specified rates. In breach of this contract, the assessee sold crackers at lower rates, to the detriment of the other parties to the contract. Consequently, the other parties filed a suit in this Court to recover the damages which they had sustained by reason of the breach of contract on the part of the assessee. The Court found that the assessee was liable in damages and assessed the sum at Rs. 5,000. With costs, the total amount payable by the assessee came to Rs. 6,203. The assessee claimed to be entitled to deduct this as a business expenditure under Section 10 (2) (xii) of the Indian Income-tax Act. This contention was rejected by the Income-tax Officer, but the Appellate Assistant Commissioner allowed it. The Income-tax Appellate Tribunal agreed with the Income-tax Officer. The assessee then asked the Tribunal to state a case for this Court as it involved a question relating to the construction of the Act. This application was granted, and consequently the Tribunal has referred to this Court the following question :

“ Whether the sum of Rs. 6,203 being costs and damages incurred in connection with an action for breach of contract is not expenditure laid out or expended wholly and exclusively for purposes of the assessee's business within the meaning of Section 10 (2) (xii) of the Act ? ”

Section 10 (2) (xii) allows the deduction of any expenditure, not being in the nature of capital expenditure or personal expenses of the

assessee, laid out or expended wholly and exclusively for the purposes of a business. In *Inland Revenue Commissioners v. Warnes & Co.*¹, Rowlatt, J., said that a loss connected with or arising out of a trade must, at any rate, amount to something in the nature of a loss which is contemplable and in the nature of a commercial loss. In that case, the respondents who were oil exporters were sued for a penalty under the Customs Consolidation Act, 1876, Section 139, as extended by the Customs (War Powers) Act, 1915, Section 5, sub-section (1), for the breach of orders and proclamations relating to the requirements of the Board of Customs and Excise with respect to a consignment of oil shipped by them to Norway. The result of the action was that the respondents were made to pay as a mitigated penalty the sum of £ 2,000 and costs, and the question was whether they were entitled to treat this as a loss connected with or arising out of the trade or business within Section 100, Schedule D, Case 1, Rule 3, of the Income-tax Act, 1842, and it was held that they were not.

The judgment of Rowlatt, J., in that case was upheld by the Court of Appeal in *Inland Revenue Commissioners v. Von Glehn*.² There a penalty of £ 3,000 was imposed upon the appellants for the breach of orders and proclamations issued under the same statutory provisions, and they sought to deduct the amount from their profits as a loss connected with or arising out of their trade. It was held that they were not entitled to do so. In the course of his judgment, Lord Sterndale, M. R., said:

"During the course of the trading this company committed a breach of the law. As I say, it has been agreed that they did not intend to do anything wrong in the sense that they willingly and knowingly sending these goods to an enemy destination: but they committed a breach of the law, and for that breach of the law they were fined. That, as it seems to me, was not a loss connected with the business, but was a fine imposed upon the company personally, so far as a company can be considered to be a person, for a breach of the law which it had committed. It is perhaps a little difficult to put the distinction into very exact language, but there seems to me to be a difference between a commercial loss in trading and a penalty imposed upon a person or a company for a breach of the law which they have committed in that trading. For that reason I think that both the decision of Rowlatt, J., in this case, and his former decision in *Inland Revenue Commissioners v. Warnes & Co.*¹, which he followed, were right, and that this appeal should be dismissed with costs."

(1) (1919) 2 K. B. 444.

(2) (1920) 2 K. B. 553.

In the present case, the assessee was not fined for a breach of law, but was made to pay damages for a breach of the contract entered into. The assessee's action in disregarding the undertaking given was palpably dishonest and we are of the opinion that the award of damages which followed did not constitute an expenditure falling within Section 10 (2) (xii). It was not incidental to the trade.

For the respondent, stress has been laid on the observations made by Scrutton, L. J., at the end of his judgment in *Inland Revenue Commissioners v. Von Glehn*¹. Scrutton, L.J., said that he did not wish to decide until he had heard the matter further argued, whether damage paid in civil proceedings in respect of carrying on business in a negligent manner can or cannot be deducted from the profits. This is not a case of conducting a business in a negligent manner; it is a case of conducting a business in a dishonest manner.

The question referred is answered in the negative and the Commissioner of Income-tax is entitled to his costs, which we fix at Rs. 250.

Reference answered in the negative.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME-TAX, BOMBAY

v.

GOKALDAS HUKUMCHAND

SIR JOHN BEAUMONT, C. J., and KANIA, J.

April 6, 1943.

FIRM—MINOR SONS—REGISTRATION OF FIRM WITH MINOR SONS WITHOUT FATHER AS PARTNERS—PERSONALITY AND BUSINESS OF FIRM CLOSELY CONNECTED WITH ANOTHER FIRM IN WHICH FATHER AND ONE MINOR SON ARE PARTNERS—WHETHER MINORS MERE NOMINEES OF FATHER—WHETHER INCOME OF MINORS DERIVED FROM FIRM INCOME OF FATHER.

The assessee and his minor son J. were partners in a firm. Subsequently a second firm was started in which the assessee was not a partner but his two minor sons J. and R. were partners along with others and it was registered under Section 26-A of the Income-tax Act showing the minor sons as partners. The Income-tax authorities found as a fact that the income of the minor sons received from the second firm was really the income of the assessee for the following reasons :—

(1) (1920) 2 K. B. 553.

(i) *The minor sons held a large interest in the second firm; (ii) the age of the minors was nine and three years respectively; (iii) the younger minor brought in no capital, though the elder brought in about Rs. 24,000 capital which was transferred from moneys standing to his credit in the first firm; (iv) the brother of the assessee who was a common partner in the two firms got a substantial salary from the first firm but did not receive any salary from the second firm; (v) the second firm was financed to a great extent by the first firm; and (vi) the businesses and the personality of the two firms were closely connected:*

Held, on a reference, that the facts relied on by the Income-tax authorities did not afford any evidence on which they could properly come to the conclusion either that the assessee was a partner in the second firm, or that the minor sons of the assessee were mere nominees of their father and that their income derived in the second firm was really his income.

Case stated under Section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay, Sind and Baluchistan: (Income-tax Reference No. 10 of 1942).

STATEMENT OF CASE.

"In compliance with your Lordships' order dated the 28th of March 1941, passed under Section 66 (3) of the Indian Income-tax Act, XI of 1922 (hereinafter referred to as "the Act"), I have the honour to refer for your Lordships' decision the question stated in paragraph 9 below, which has been held to arise from the assessment of Mr. Gokaldas Hakamchand (hereinafter referred to as "the assessee") for the year 1939-40, the relevant accounting period being the Sanvat year 1994.

2. **Facts of the Case.**—The assessee is a partner in the firm of Messrs. Lallubhai Amichand (hereinafter referred to as "the first firm") whose business consists of the manufacture and sale of metal utensils of various kinds. The constitution of this firm is as follows:—

| | Rs. | A. | P. |
|-------------------------|-----|----|-----|
| 1. Gokaldas Hakamchand | ... | 0 | 4 6 |
| 2. Jagmohandas Gokaldas | ... | 0 | 3 6 |
| 3. Vithaldas Hakamchand | ... | 0 | 4 6 |
| 4. Tulsidas Vithaldas | ... | 0 | 1 3 |
| 5. Motichand Amichand | ... | 0 | 1 0 |
| 6. Wadilal Manilal | ... | 0 | 1 3 |

Partner No. 2, Jagmohandas Gokaldas, is a minor son of the assessee. Partner No. 3, Vithaldas Hakamchand, is a brother of the assessee. The amounts of profit falling to the share of the minor, Jagmohandas Gokaldas, have been credited annually to his account in the books of

the firm, but since the assessment for 1937-38 they have been included in the income of the assessee for assessment purposes under sub-section (3) of Section 16 of the Act which was added by the Income-tax (Amendment) Act, 1937.

3. During the Samvat year 1994 (assessment year 1939-40) a new firm (hereinafter referred to as "the second firm") was started under the name of Rameshchandra & Co. This firm purchases and sells raw materials such as copper and brass rods and pipes.

The constitution of the second firm is as follows :—

| | Rs. | A. | P. |
|---------------------------|-----|----|-----|
| 1. Jagmohandas Gokaldas | ... | 0 | 5 9 |
| 2. Rameshchandra Gokaldas | ... | 0 | 5 9 |
| 3. Vithaldas Hakamchand | ... | 0 | 1 0 |
| 4. Gokaldas Vithaldas | ... | 0 | 1 3 |
| 5. Brijlal Manilal | ... | 0 | 1 3 |
| 6. Motichand Amichand | ... | 0 | 1 0 |

Partner No. 1 is identical with partner No. 2 in the first firm and as has already been stated he is a minor son of the assessee. Partner No. 2 is also a minor son of the assessee. Partner No. 3 is identical with partner No. 3 in the first firm and is a brother of the assessee. Partner No. 4 is a brother of partner No. 4 in the first firm and partner No. 5 is a brother of partner No. 6 in the first firm. Partner No. 6 is identical with partner No. 5 in the first firm. The shares of the first three partners in each firm amount to 12 as. 6 ps., and the shares of the other three partners in each firm amount to 3 as. 6 ps.

4. The balance sheet of the second firm, as at Diwali 1994, shows total liabilities and capital amounting to Rs. 1,56,197, which consists mainly of the following accounts :—

| | | |
|-----------------------------|-----|--------------|
| Mangaldas Kalidas | ... | Rs. 43,311 |
| Jagmohan Kanchanalal | ... | „ 87,365 |
| Jagmohan Gokaldas (Partner) | ... | „ 24,274 |
| | | <hr/> |
| | | Rs. 1,54,950 |

The deposits of Mangaldas Kalidas and Jagmohan Kanchanalal, who are not partners, were transferred from their accounts with the first firm. The capital contributed by the minor partner Jagmohan Gokaldas was also transferred from his account in the first firm. The other minor partner, Rameshchandra Gokaldas, who gives his name to the second firm, has not brought in any capital.

5. In the partnership deed of the first firm, dated the 28th of January 1938, of which a copy is annexed as Exhibit A it is provided

that " the minor, Jagmohan Gokaldas, shall be entitled to the benefits of the partnership only and shall not be made personally liable to any obligation of the said firm of Messrs. Lallubhai Amichand & Co., but his respective share only in profits of the said firm, and pending his attaining the age of majority the share of the minor in the profits of the business of the firm shall accumulate to the credit of the minor so as to be available to meet his respective share in losses if any, incurred by the firm at any time during the minority ". In the partnership deed of the second firm (Exhibit B) it is provided that all the partners including the minors " shall bear and be liable to all losses suffered by the partnership business in the same proportions in which they are entitled to profits as aforesaid ". Thus the minors are not treated as being merely entitled to the benefits of the partnership as in the case of the first firm. The partnership deed of the second firm has been signed by the assessee on behalf of the two minor partners.

6. For the assessment year 1939-40 the Income-tax Officer, C-III Ward, Bombay, assessed the total income of the assessee at Rs. 1,26,181. In computing this income he included a sum of Rs. 1,600 being the shares of the minor partners in the profits of the second firm, on the ground that these profits were in reality the profits of the assessee. A copy of the assessment order is annexed and marked C.

7. Against this order the assessee appealed to the Appellate Assistant Commissioner, A-Range, Bombay. In the course of the appellate proceedings he filed two affidavits, of which one is signed by himself and states that he had no personal interest whatsoever in the second firm and that his sons, Jogmohan and Rameshchandra, were not his nominees, but were admitted to the benefits of partnership in the firm in their individual capacities. The second affidavit supports this statement and is signed by the other four partners of the second firm. Copies of the affidavits are annexed as exhibits D and E. The Appellate Assistant Commissioner, after considering these affidavits and hearing the assessee, agreed with the conclusion reached by the Income-tax Officer and rejected the appeal. A copy of his order is annexed as exhibit F.

8. The assessee then submitted applications to the Commissioner under Sections 33 and 66 (2) of the Act requesting him to revise the assessment or in the alternative to make a reference to the High Court. My predecessor rejected both of these applications holding that the material before the Appellate Assistant Commissioner was sufficient to justify the finding of fact at which he arrived, and that there were no grounds for a reference to the High Court. Copies of his orders are annexed as exhibits G and H.

9. **Question for decision.**—The assessee then submitted an application to the High Court under Section 66 (3) and as a result of that application I have been directed to refer the following question :—

“ Whether there was any evidence before the Income-tax Officer and/or the Appellate Assistant Commissioner so as to warrant the views each of them has taken namely that the said sum of Rs. 1,600 being the share of the minors in the profits of the said firm of Rameshchandra & Co., for the Samvat year 1994 could be said to be the income of the petitioner so as to include it in his total income for the said year.”

10. **Opinion of the Commissioner.**—The evidence on which the Appellate Assistant Commissioner's decision was based can be briefly summarised as follows :—

(1) As has already been stated the partners in the second firm are very closely related to the partners in the first firm and in each case the shares held by the assessee and/or his brother and minor sons amount to 12 as. 6 ps. In the first firm the shares of the assessee and his minor son, Jagmohandas, amount to 8 annas and the assessee's brother, Vithaldas, holds $4\frac{1}{2}$ annas, while in the second firm the assessee's two minor sons hold $11\frac{1}{2}$ annas and Vithaldas holds only one anna.

(2) Neither of the minor sons is in a position to take any part in the management of the second firm and one of them contributed no capital. It is argued on behalf of the assessee that the shares of the minor sons were given to them out of the natural love and affection of the other partners. The outside partners, however, whose share amounts to 3 annas 6 pies could have no such natural love and affection for the minors. The only remaining partner is their uncle, Vithaldas, who has a one anna share, and it seems unlikely that he could have given the minors their predominant share in the partnership. He has himself contributed no capital to the second firm and there is nothing to indicate that he has a controlling influence because of his labour and skill. Indeed it appears that he devotes most of his time to the first firm, since in the Samvat year 1994 and also in subsequent years he has been paid a salary of Rs. 4,200 for the management of that firm, but he has been paid no salary by the second firm. The assessee on the other hand receives no salary from the first firm and appears to be free to devote his attention to the second firm.

(3) In the partnership deed of the first firm (exhibit A) it was expressly provided that pending the attainment of his majority the share of the minor partner, Jagmohandas, in the profits should be accumulated so that they might be available to cover his share of any

losses which might be incurred during his minority. It is however an admitted fact that Rs. 23,889-8-0 were withdrawn from the minor's account and transferred to form part of the capital of the second firm. The assessee has stated that this was done with the consent of all the partners. There is however no writing varying the provision in the partnership deed and it does not appear that the assessee has any authority to consent to such a variation on behalf of the minor partner.

(4) In the partnership deed of the second firm (exhibit B) it is stated that the partnership "commenced from the sixth day of Vaisakh Sud Samvat year 1994" (*i.e.*, 5th May 1938) but the deed was not drawn up until the 22nd of August 1939, after a notice had been issued to the assessee calling for a return of his income for the assessment year 1939-40. Moreover the deed was drafted so superficially that the minors were shown as entering into the partnership through their guardian although under Section 30 of the Indian Partnership Act, 1932, they cannot become partners but can only be admitted to the benefits of partnership.

(5) The second firm has been entirely financed by transfers of capital from the first firm, and it seems clear that the second firm could not have established itself in business without the support and backing of the first firm.

(6) The business of the second firm is to purchase raw materials of the type required by the first firm for the manufacture of utensils. There is thus an obvious connection between the two firms. Moreover the premises of the two firms are situated on the opposite sides of the same road and they use the same telegraphic address "Cycle Brand." This last point is of considerable significance since the existence of a common telegraphic address seems clearly to indicate that the one firm has no business secrets from the other.

11. I submit that it is reasonable to conclude from the above facts that the partnership deed of the second firm is an ad hoc document prepared mainly for income-tax purposes, that the second firm is entirely subsidiary to, and controlled by, the first firm, that the assessee himself has in fact a predominant position in both firms, and that he is responsible for the allocation of shares in the second firm to his minor sons. Against these conclusions the assessee has produced no evidence apart from the two affidavits (exhibits E and F) signed by himself and by the other partners in the second firm. Such affidavits are not in themselves sufficient to disprove the conclusions which can reasonably be drawn from the known facts of the case. Moreover it is obvious from the constitution of the firms as stated in paragraphs 2 and 3 above that the assessee and the

members of his family have a controlling interest in both firms and in these circumstances the other partners cannot be regarded as independent witnesses.

12. It was in the interest of the assessee to keep his own name out of the partnership of the second firm, since if he had been shown as holding any share in that firm the shares of the minor sons would have been clearly assessable in his hands under Section 16 (3) of the Act. Every assessee is of course entitled to adopt any legal measures which may be open to him for the purpose of reducing the incidence of taxation, but the income-tax authorities on their part are entitled to demand proof that the ostensible position is in accordance with the facts. I submit that this has not been proved in the present case and that there is evidence to justify the Appellate Assistant Commissioner's finding that the shares of the minors in the profits of the second firm were in reality the income of the assessee. I am therefore of the opinion that the question which has been stated should be answered in the affirmative."

Sir Jamshedji Kanga with R. J. Kolah, for the Assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

BEAUMONT, C.J.—This is a reference made by the Commissioner of Income-tax raising the following question:—

"Whether there was any evidence before the Income-tax Officer and/or the Appellate Assistant Commissioner so as to warrant the views each of them has taken, namely, that the said sum of Rs. 1,600 being the share of the minors in the profits of the said firm of Rameshchandra & Co., for the Samvat year 1994 could be said to be the income of the petitioner so as to include it in his total income for the said year."

The facts are that there is a firm of Lallubhai Amichand in which the present assessee and his minor son Jagmohandas are partners, and there are four other partners, namely the brother of the assessee and three outside parties. So far as regards that, it is clear that under Section 16 (3) of the Income-tax Act the income of the minor son can be included in the income of the assessee, because the assessee is a partner in that firm. Then there is a second firm which was started either in the year 1938 or 1939. It is suggested that it was May 1938, but the partnership deed was only registered in 1939; the exact date at which it was started is irrelevant. In that firm the assessee is not a partner, but his minor son Jagmohandas is a partner, and so is his second minor son Rameshchandra. His brother, who is a partner in

the first firm is a partner in the second firm ; and one of the outside parties, who is a partner in the first firm is a partner also in the second firm ; and a brother of each of the other two outside parties, who are partners of the first firm, is a partner in the second firm. So that obviously the personality of the two firms is very closely associated. On the finding of the Commissioner their businesses are also closely associated. But the question is whether the income derived by the two minor sons of the assessee from the second firm can be included in the income of the assessee, their father. It is not suggested that Section 16 (3) of the Income-tax Act applies, because the assessee is not a partner in the second firm, as he must be in order to bring that section into operation. But the Income-tax Officer found as a fact that the income of the two minor sons derived from the second firm is really the income of the assessee, and the question is whether there is any evidence to support that finding.

I may mention that the second firm was registered under Section 26A of the Income-tax Act showing the minor sons as partners, and, therefore, they fall to be assessed under Section 23 (5). But I will assume that, so far as registration is concerned, it would be open to the Income-tax Officer to treat the income of the minors as part of the income of the assessee.

The facts relied on as justifying the finding of the Income-tax Officer, which was confirmed, as is usual, by the Assistant Commissioner, and subsequently adopted by the Commissioner, are: first, the large interests which the minors had in the second firm ; they had 11 annas share in the rupee ; secondly, the age of the minors, which is nine years and three years respectively ; thirdly, the younger minor brought in no capital, though the elder minor brought in about Rs. 24,000 capital which was transferred from moneys standing to his credit in the first firm ; fourthly, the uncle, who is a common partner in the two firms, gets a substantial salary from the first firm, but is not shown to receive any salary from the second firm ; fifthly, the second firm was financed, at any rate to a very great extent, by the first firm ; sixthly, the businesses of the two firms are closely connected, and the personality of the two firms is, as I have mentioned, also closely connected. Now, all those facts undoubtedly give rise to a suspicion that the two minor sons are really nothing but nominees of the assessee. The question really is whether those facts not only give rise to a suspicion, but justify the inference of fact drawn by the Income-tax Officer that the minors were mere nominees of the assessee. I do not think that they do justify such an inference, though they certainly give rise to suspicion. The evidence consisting of two affidavits

by the assessee and the other partners in the second firm shows that the assessee had no interest in the second firm. Not unnaturally, the books of the second firm do not show that the shares of the minors have been carried to the credit of the assessee. That may be natural enough, but still the facts that the evidence produced is biased and that the other evidence is easily accounted for does not provide evidence, and there is no evidence whatever that the assessee took any part in the business of the second firm. No doubt, the two firms are closely connected, but that cannot justify us in holding that the assessee, having a share in the first firm, must necessarily have had a share in the second firm. In my opinion, all the facts relied on by the Commissioner do not afford any evidence on which he could properly come to the conclusion either that the assessee is a partner in the second firm, or that the minor sons of the assessee are mere nominees of their father, and that their income derived in the second firm is really his income.

Therefore, we must answer the question in the negative. The Commissioner to pay costs.

KANIA, J.—I agree.

Reference answered in the negative.

[IN THE MADRAS HIGH COURT].

COMMISSIONER OF INCOME TAX, MADRAS

v.

CT. RM. N. NARAYANAN CHETTIAR.

SIR LIONEL LEACH, C.J., and LAKSHMANA RAO, J.

July 30, 1948.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 3—‘INCOME’—INTEREST AND DAMAGES FOR WRONGFUL DETENTION OF MONEY—DIFFERENCE—DEATH OF PARTNER LEAVING MINOR SONS—DECEASED PARTNER’S SHARE OF CAPITAL PAID TO SONS ONLY ON ATTAINMENT OF MAJORITY WITH INTEREST FIXED BY PANCHAYATDARS—INTEREST RECEIVED, WHETHER DAMAGES FOR WRONGFUL DETENTION OF MONEY OR ‘INTEREST’—ASSESSABILITY.

The assessee’s father who was a partner in a money-lending firm died in 1921, and some years after his death a panchayat fixed the amount due to the assessee and his brother on account of their father’s share at \$ 1,55,900. Being minors, the amount was not paid to them till 1938, when another panchayat decided that in addition to the above sum a further sum of \$ 27,000 should be paid to them on account of interest, and the assessee received a sum of Rs. 21,153 as his share in the amount thus paid : Held, that the sum of Rs. 21,153 received by the assessee was

interest and not damages for wrongful detention of money and was therefore assessable to income-tax.

Commissioner of Income-tax, Bihar and Orissa v. Rani Prayag Kumari Debi [1940] (*I.L.R.* 10 Pat. 186; 8 *I.T.R.* 25) referred to; *Behari Lal Bhargava v. Commissioner of Income-tax* [1941] (*I.L.R.* 1941 All. 54; 9 *I.T.R.* 9) doubted.

Cases referred to;

Behari Lal Bhargava v. Commissioner of Income-tax (1941) *I.L.R.* 1941 All. 54; 9 *I.T.R.* 9.

Commissioner of Income-tax, Bihar and Orissa v. Rani Prayag Kumari Debi (1940) *I.L.R.* 10 Pat. 186; 8 *I.T.R.* 25; 186 *I.C.* 263; *A.I.R.* 1939 Pat. 662.

Commissioners of Inland Revenue v. Barnato (1936) 20 *Tax Cas.* 455.

Schulze v. S. W. Bensted (1915) 7 *Tax Cas.* 30; 1916 *Sess. Cas.* 188; 53 *Sc. L.R.* 156
Vyse v. Foster 8 *Ch.* 309.

Case Referred No. 11 of 1943.

Case referred to the Madras High Court by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by Section 92 of the Indian Income-tax (Amendment) Act (VII of 1939) in Application No. 66 R.A. No. 4—Madras of 1941-42 on its file for decision on the following question of law, *viz.*—

“Whether, having regard to the circumstances of the case, the conclusion of the Bench, *viz.*, that the amount of Rs. 21,153 received by the appellant was in the nature of damages for wrongful detention of the money in the hands of the partner of the appellant's father and therefore not assessable, is correct in law?”

Under Section 33 of the Indian Income-tax Act (XI of 1922), the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. VERMA (Judicial Member) and P. N. S. AIYAR (Accountant Member) delivered the following Judgment on 21st August 1941.

JUDGMENT OF APPELLATE TRIBUNAL.

“This appeal refers to the assessment year 1939-40 and is in respect of an item of Rs. 21,153. The appellant claims that out of the total income of Rs. 28,396 assessed by the Income-tax Officer and confirmed by the Appellate Assistant Commissioner a sum of Rs. 21,153 should be deducted on the ground that this item is not income.

2. The facts are that the appellant's father had a share in M. S. M. M. firm at Ipoh and Sithiwan. The firm's property included certain lands known as Chengkat Meranti Estate at Sithiwan and Hill Rise Estate at Batukajah. The appellant's father died in 1921 and on his death the partnership came to an end. It is said that a Panchayat was set up in 1928 which appears to have determined the amount to be paid to the appellant and his brother on account of their father's share of capital, surplus capital and profits in the firm. The award is not

available to us nor any proceedings of the said Panchayat. The Income-tax Officer however examined Mr. M. S. S. Chidambaram Chettiar one of the Panchayatdars in this award and found from him that a sum of \$ 1,55,900 was awarded to be paid to the appellant and his brother. This sum thus arrived at in favour of the appellant and his brother was not paid to them on account of their minority till the year 1938, when all of them became majors. Another Panchayat again went into the question and in addition to the original sum a further sum of \$ 27,294 was awarded by way of interest. It is not agreed between the parties that this sum was awarded as interest and we shall have to consider this question a little later.

3. The partner thereafter gave a hundi on the 2nd April 1938 on his Ipoh shop for a sum of \$ 1,82,900 and a deed of release was executed by the appellant, his brother, and their adoptive mother in favour of M. S. M. M. Firm. The hundi was sent to Ipoh for collection and it was cashed on the 9th May, 1938, and a further sum of \$ 294 in interest from the date of the hundi to the date of encashment was also realised. The total amount of interest realised was \$ 27,294 and the half share of the appellant came to \$ 13,647 equivalent to Rs. 21,153 which is the sum in dispute before us.

4. The Income-tax Officer treated this sum as interest received in the previous year and the following two contentions are urged before us:—

(1) This sum of Rs. 21,153 is not interest. It is a part of the capital.

(2) If it is to be treated as interest, it was not received on the date of encashment of the hundi 9th May 1938, but the amount should be deemed to have been received on 2nd April 1938, the date on which the hundi was handed over to the appellant and the release deed was executed in favour of the debtors.

5. If we hold that the date of cashing of the hundi is to be taken as the date of the receipt, then it is within the year of account as the date of the closing of the "previous year" is 2nd April 1938.

6. The representative of the appellant who appeared before us in this case relied on *L. C. T. S. P. Subramanyam Chettiar v. Commissioner of Income-tax, Madras*¹, in support of the argument that the debt should be deemed to be discharged on the date on which the hundi was executed and not on the date on which it was cashed and also on V Income-tax Reports p. 534, the case of *Ar. Pl. Sp. Manickam Chettiar v. Commissioner of Income-tax, Madras*. In V Income-tax Reports at page 534 it was laid down that when the assessee

(1) (1935) 3 I.T.R. 346.

accepted the jewels and took an assigned decree, the debt to the Penang business was completely discharged and the assets of their business were diminished by the amount the equivalent of which was taken in kind and there was a corresponding increase in the assessee's assets in British India and that the transaction in the face of the facts of the case must be held to be a remittance into British India. We do not think that these cases apply to the facts of the case before us and we have a decision of their Lordships of the Privy Council in the case of the *Maharaja of Darbhanga v. Commissioner of Income-tax*¹, reported in 6 I.T.C. at p. 401, and at pages 409-10 their Lordships have considered the question. It was held in this case that where a liability is discharged by the debtors' own promissory notes it cannot be said to be equivalent to cash. A debtor who gives his creditor a promissory note for the sum he owes can in no sense be said to pay his creditor but merely gives him a voucher or voucher of debt possessing certain legal attributes. In this case merely a hundi was given payable outside British India on demand. The hundi will not mature into a payable debt until a demand was made and was in fact an inchoate liability maturing only on demand being made from the person on whom the hundi was drawn and is only discharged when the amount is paid. It cannot, therefore, be said that on the day the appellant received the hundi he received a right to make a demand on the person on whom the hundi was drawn and who was liable to pay the amount. We think therefore that the date of payment is the actual date on which the money can be said to have been received by the appellant and was rightly treated as received on the date of the amount in cash.

7. The representative appearing for the appellant also argued that the amount received was by way of damages but he was not able to support his case with any authority. The mere argument that the sum is of capital nature does not find favour with us. The appellant should not suffer for want of presentation of his case or for the erroneous view he takes the amount being capital but we think that on the view of law expressed in decided cases it will not be just to the appellant if we do not refer to the relevant cases which are within our knowledge and which make the sum in question not liable to tax.

8. We think that the amount of Rs. 21,153 received by the appellant was in the nature of damages for wrongful detention of the money in the hands of the partner of the appellant's father. If he had paid the amount in 1928 he would not have been liable for this extra sum which the Panchayatdars decided to award against them. Such an amount awarded as damages has been held in several cases as not liable to

income-tax. We may refer here to the case of *Commissioner of Income-tax, Bihar and Orissâ v. Rani Prayag Kumari Debi* reported in 7 I.T.R. 25. The widow of a deceased holder of an impartible Raj instituted a suit for the recovery of all the moveables and immoveables left by the deceased holder against a collateral of the latter, who had taken possession of them. In 1933 a decree was passed awarding to the widow :—(1) a number of moveables ; (2) the value of moveables as could not be returned ; (3) damages to the extent of 22 lakhs for wrongful detention of them. The question arose when in the accounting year the Rani received Rs. 62,500 out of the damages awarded, and it was held that the damages were received for wrongful detention of the moveable properties and there was not any contract to pay interest and it was not, therefore, within Section 3 of the Indian Income-tax Act read with Section 4 (3) (vii). We think that this case is fully applicable to the facts of the case before us and here also the sum of Rs. 21,153 was paid for wrongful detention of the money and the amount is of a casual and non-recurring nature and not liable to tax.

9. There is also the latest case reported in 1941 I.T.R. at page 9 in the case of *Behari Lal Bhargava v. Commissioner of Income-tax, C.P. & U.P.*, where a Full Bench of the Allahabad High Court decided that the interest awarded under Section 28 of the Land Acquisition Act was in the nature of compensation for the loss of the assessee's father's right to retain possession of the property acquired. It was held to be damages assessed in terms of interest for the loss of possession of property up to the date of the receipt of its consideration and it was held not to be an income and was not assessable to tax. In the case before us it cannot be said that this interest was income made in the course of business. It was not contractual interest but merely damages the measure of which was the amount awarded and though it may be called interest, as damages it is not liable to assessment.

10. We, therefore, allow this appeal and set aside the assessment of the sum of Rs. 21,153."

On the application of the Commissioner under Section 66 (1) of the Income-tax Act, the Income-tax Appellate Tribunal referred the case to the Madras High Court.

STATEMENT OF CASE.

"This is an application of the Commissioner of Income-tax, Madras, asking reference of the following question of law to the High Court of Judicature at Madras :—

“ Whether having regard to the circumstances of the case, the conclusion of the Bench, *viz.*, that the amount of Rs. 21,153 received by the appellant was in the nature of damages for wrongful detention of the money in the hands of the partner of the appellant's father and, therefore not assessable, is correct in law ? ”

2. The respondent, in his reply, has denied that any question of law arises. The respondent admits that the decision of the Tribunal is correct in law and that the applicant indirectly seeks to get another appeal to the High Court on a question of fact which is not sanctioned by law. We consider that the respondent is not right. He does not seem to appreciate the difference between a question of law and a question of fact. We think that the case should be stated to the High Court for their opinion on the question formulated by the applicant.

3. This Bench of the Tribunal decided on 28th August 1941 in appeal R.A.A. No. 15/Madras of 1941-42, that the income of Rs. 21,153 sought to be taxed by the Department was actually not an income taxable. It was held that it was in the nature of damages for wrongful detention of the money in the hands of the partner of the appellant's father and on the authorities of the cases reported in *Commissioner of Income-tax, Bihar & Orissa v. Rani Prayag Kumari Devi*¹ and *Behari Lal Bhargava v. Commissioner of Income-tax, C.P. & U.P.*², the appeal was allowed. The applicant has stated that the findings of fact which have been arrived at by the Tribunal are right but he only seeks reference on the question of law arising from the findings of facts. The findings arrived at by the Tribunal were as below and represent facts on which the question of law arises :—

(i) The appellant's father had a share in M.S.M.M. Firm at Ipoh and Sithiawan.

(ii) The appellant's father died in 1921 and so the partnership came to an end by that time.

(iii) A panchayat was set up in 1928 and it determined the amount to be paid to the appellant and his brother on account of their father's share of capital, surplus capital and profits in the firm at \$ 1,55,900.

(iv) The amount was not paid to them on account of their minority till the year 1938.

(v) In 1938 when they became majors another panchayat went into the question and decided that in addition to the above sum of \$ 1,55,900 a further sum of \$ 27,294 should be paid on account of interest.

(1) (1940) 8 I.T.R. 25.

(2) (1941) 9 I.T.R. 9.

(vi) A hundi for the sum of \$ 1,82,900 was given on 2nd April 1938 and the appellant and his brother executed release deeds and the hundi was cashed on 9th May 1938.

The reasons which led this Bench of the Tribunal to come to this decision are mentioned in its order, dated 28th August 1941 in appeal K.A.A. No. 15—Madras of 1941-42 and need not be repeated here.

4. We therefore refer the following question of law for the opinion of the High Court of Judicature at Madras :—

Question of Law referred.—Whether, having regard to the circumstances of the case, the conclusion of the Bench, *viz.*, that the amount of Rs. 21,153 received by the appellant was in the nature of damages for wrongful detention of the money in the hands of the partner of the appellant's father and therefore, not assessable, is correct in law ?

5. The papers mentioned in the index attached will form the paper book in this case."

K. V. Sesha Ayyangar, for the Commissioner.

T. P. Gopalakrishna Ayyar, for the assessee.

JUDGMENT.

(Judgment of the Court was delivered by the Hon'ble the Chief Justice.)

This is a reference by the Income-tax Appellate Tribunal, Calcutta Bench, under Section 66 (1) of the Income-tax Act, and has been made at the instance of the Commissioner of Income-tax, Madras. The assessee's father, who died in 1921, was a partner in a money-lending firm carried on in the Federated Malay States. Notwithstanding the death of the assessee's father, the business of the firm was carried on until 1928 when a panchayat met to decide what was payable to the assessee and his brother on account of their father's share, and the amount was fixed at \$ 1,55,900. The assessee and his brother were minors, and so was Meyyappa. Ten years later, another panchayat was formed for the purpose of deciding what interest should be paid on the \$ 1,55,900 and the panchayatdars fixed the amount at \$ 27,000. A sum of \$ 1,82,900 representing principal and interest, was paid to the assessee and his brother by way of a hundi on the 2nd April 1938, the hundi being cashed on the 9th May 1938. The assessee's share of the interest came to Rs. 21,153. The Income-tax Officer included this sum as income of the assessee for the year 1939-40 and the assessee objected. He contended that the Rs. 21,153 represented damages paid to him for the wrongful detention of the principal sum to which he was entitled under the award of the first panchayat. This contention was

accepted by the Income-tax Appellate Tribunal, but as the decision involved a question of law, it has referred to this Court for decision the following question:—

“Whether, having regard to the circumstances of the case, the conclusion of the Bench, *viz.*, that the amount of Rs. 21,153 received by the appellant was in the nature of damages for wrongful detention of the money in the hands of the partner of the appellant's father and therefore, not assessable, is correct in law?”

In accepting the assessee's contention that this sum represented damages for the wrongful detention of the principal, the Tribunal relied on two cases, *Commissioner of Income-tax, Bihar & Orissa v. Rani Prayag Kumari Debi*¹ and *Behari Lal Bhargava v. Commissioner of Income-tax*.² In our judgment, these cases are not in point, and in any event the correctness of the decision in the second case is open to doubt. The first case had reference to a sum which had been awarded to the assessee in a civil suit as damages for the wrongful detention of her moveable property. The Patna High Court held that as the amount was decreed as damages, it was not a source of income within the contemplation of the Act. The second case was decided by the Allahabad High Court. There an amount awarded as compensation in land acquisition proceedings carried interest, and the question was whether the interest represented assessable income. The Allahabad High Court held that it did not, but with great respect we find ourselves unable to follow the reasoning. Certainly we are not prepared to accept the judgment as a guide to the decision in the present case.

There are two cases which we consider have bearing here, namely, *Schulze v. S. W. Bensted*³ and *Commissioners of Inland Revenue v. Barnato*⁴. In *Schulze v. S. W. Bensted*³ the appellant, who was the trustee of an estate, sued the representatives of a deceased trustee for damages to the estate caused by his negligence, and a decree was passed directing the defendants to pay a sum of money with interest thereon at the rate of $3\frac{1}{2}$ per cent. per annum from the date on which the sum should have belonged to the estate. The Surveyor of Taxes claimed that the interest represented income, but this claim was resisted. The Court of Session held that the Surveyor of Taxes was right. In *Commissioners of Inland Revenue v. Barnato*³, the decision in *Schulze v. S. W. Bensted*⁴ was approved by the Court of Appeal in England. In that case, the respondent inherited certain sums in a business which vested in him on attaining majority. After he had attained majority, he became a partner in the firm, but soon afterwards the partnership was

(1) (1940) I. L. R. 19 Pat. 186 ; 8 I. T. R. 25.

(2) (1941) I. L. R. 1941 All. 54 ; 9 I. T. R. 9.

(3) (1915) 7 Tax Cas. 30.

(4) (1936) 20 Tax Cas. 455.

dissolved, and it was agreed that certain securities should be transferred to the respondent and certain sums of money paid over to him. He was in fact paid three sums of money. On the 1st April 1925, he was paid £ 2,00,000, on the 21st April 1926, £ 3,50,000, and between the 26th April and 23rd June 1927, £ 3,27,250. It was found as a fact that these sums, although described as capital sums, did represent interest in part. The question was whether the respondent was liable to be taxed in respect of the interest portion. It was held that he was. In his judgment Romer, L. J., said :—

“If he (respondent) had elected to take profits I cannot see how it could be suggested for a moment that any profits he so recovered could be regarded in any shape or form as damages. As we know, in the end he elected to take interest in lieu of profits. But any interest that the trustees were directed to pay him in addition to the principal sum would not be damages. As pointed out by James, L. J., in *Vyse v. Foster*¹, the Court of equity did not punish trustees who had failed to perform their trust; the trustees would be ordered to pay the interest because in the eyes of equity that interest belonged to the plaintiff; it was interest which had been earned, or must be deemed to have been earned, by the trustees by the use of the Plaintiff's money.”

We hold that the sum of Rs. 21,153 represented interest and not damages for the wrongful detention of money. Accordingly the answer to the question referred is that the Appellate Tribunal erred in holding that the sum represented damages. The Commissioner succeeds and he will have his costs Rs. 250.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

EXECUTORS OF SARDAR NARAIN SINGH, *In re.*

DIN MOHAMMAD and SALE, JJ.

May 19, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 10 (2) (xii), 12—
BUSINESS EXPENDITURE—DIRECTOR OF COMPANY—MISFEASANCE PRO-
CEEDINGS AGAINST DIRECTOR IN COURT OF LIQUIDATION—AMOUNT
CONTRIBUTED TO ASSETS OF COMPANY BY WAY OF COMPENSATION—
WHETHER ALLOWABLE DEDUCTION—INDIAN COMPANIES ACT (VII OF
1913), SEC. 235 (1).

(1) 3 Ch. 309 at 333.

In the course of the liquidation of a Bank the Official Liquidator submitted claims against the directors under Section 235 of the Indian Companies Act on the ground that they had been guilty of a misfeasance in signing balance sheets, which they knew to be incorrect. The claim against a director was eventually settled by payment of Rs. 35,000 and the executors of the director's estate claimed the amount as a deduction against the income of the year in which it was paid:

Held, that under the circumstances the sum of Rs. 35,000 was not allowable either under the provisions of Section 10 or Section 12 of the Indian Income-tax Act, 1922.

Cases referred to;

Commissioners of Inland Revenue *v.* Alexander Von Glehn & Co. Ltd [1920] 12 Tax Cas. 332; (1920) 2 K. B. 553; 89 L. J. K. B. 590; 123 L. T. 125; 35 T. L. R. 463.

Amrita Bazar Patrika, *In re* [1937] 5 I. T. R. 648.

Commissioner of Income-tax, Burma *v.* Gasper & Co., Rangoon [1940] 8 I. T. R. 100.

Kangra Valley Slate Company Ltd *v.* Commissioner of Income-tax, Punjab [1935] I. L. R. 16 Lah. 479; 3 I. T. R. 324; 7 I. T. C. 375.

Lachmi Narain Gadodia *v.* Commissioner of Income-tax, Punjab [1934] I. L. R. 16 Lah. 494; 2 I. T. R. 322; 7 I. T. C. 393.

Ramaswami Chettiar and others *v.* Commissioner of Income-tax [1930] A. I. R. 1930 Mad. 808; 59 M. L. J. 403; 32 L. W. 287; 127 I. C. 611; 4 I. T. C. 438.

Case stated under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Punjab, N. W. F. and Delhi Provinces: (Civil Reference Case No. 4 of 1941).

STATEMENT OF CASE.

Facts of the case.—The late Rai Bahadur Sardar Narain Singh was one of the directors of the People's Bank of Northern India. After the bank had gone into liquidation the Official Liquidator submitted claims against the directors under Section 235 of the Indian Companies Act on the ground that they had been guilty of a misfeasance in signing balance sheets which they knew to be incorrect. The claim against the Rai Bahadur was eventually settled by the payment of a sum of Rs. 35,000 to the Official Liquidator. This payment was made during the year under assessment and the executors of the estate claimed the amount as a deduction against the income of the year. The Income-tax Officer held that the deduction was inadmissible and his decision was confirmed by the Assistant Commissioner on appeal. The relevant extracts from their orders are appended as exhibits 'A' and 'B'.

Question for consideration.—Being dissatisfied with the Assistant Commissioner's order the executors have submitted an application under Section 66 (2) of the Income-tax Act in which they have asked me to refer the following question to the High Court:—

dissolved, and it was agreed that certain securities should be transferred to the respondent and certain sums of money paid over to him. He was in fact paid three sums of money. On the 1st April 1925, he was paid £ 2,00,000, on the 21st April 1926, £ 3,50,000, and between the 26th April and 23rd June 1927, £ 3,27,250. It was found as a fact that these sums, although described as capital sums, did represent interest in part. The question was whether the respondent was liable to be taxed in respect of the interest portion. It was held that he was. In his judgment Romer, L. J., said :—

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[IN THE LAHORE HIGH COURT.]

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DIN MOHAMMAD and SALE, JJ.

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CEEDINGS AGAINST DIRECTOR IN COURT OF LIQUIDATION—AMOUNT
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Held, that under the circumstances the sum of Rs. 35,000 was not allowable either under the provisions of Section 10 or Section 12 of the Indian Income-tax Act, 1922.

Cases referred to :

Commissioners of Inland Revenue *v.* Alexander Von Glehn & Co. Ltd [1920] 12 Tax Cas. 332 ; (1920) 2 K. B. 553 ; 89 L. J. K. B. 590 ; 123 L. T. 125 ; 35 T. L. R. 463.

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Question for consideration.—Being dissatisfied with the Assistant Commissioner's order the executors have submitted an application under Section 66 (2) of the Income-tax Act in which they have asked me to refer the following question to the High Court :—

“ Whether, in the circumstances of the case, the sum of Rs. 85,000 claimed as a deduction is allowable or not under the provisions of Sections 10 and 12 of the Indian Income-tax Act, 1922.”

A copy of the application is appended as exhibit ‘ C ’.

Opinion of the Commissioner.—Section 10 of the Income-tax Act relates to income from business, profession or vocation and Section 12 relates to income from “ other sources ”. Income received from directors’ fees is normally assessed under Section 12 and the latter would therefore appear to be the appropriate section in the present case. The point is however of no practical importance since the provisions of clause (xii) of sub-section (2) of Section 10 and those of sub-section (2) of Section 12 are almost identical. Sub-section (2) of Section 12 states that “ such income, profits and gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains.” The admissibility of the deduction depends on whether it can be held to satisfy these conditions. In this connection I venture to invite a reference to the case of the *Commissioners of Inland Revenue v. Alexander Von Glehn & Co., Ltd.* (12 Tax Cases 232) where it was held that a compromise penalty paid by the assessee-company in respect of a breach of the Customs Act, 1915, was not an admissible deduction for Income-tax purposes. The Master of the Rolls (Lord Sterndale) expressed his conclusion as follows :—

“ Now, what is the position here? This business could perfectly well be carried on without any infraction of the law at all. This penalty was imposed because of an infraction of the law and that does not seem to me to be disbursement or expense which was laid out or expended for the purpose of such trade, manufacture, adventure or concern.”

Following the above ruling the Calcutta High Court refused to allow as a deduction the expenses incurred by a newspaper in defending the editor and printer and publisher in an action for contempt of Court—1937 I. T. R., 648. In my opinion the circumstances of the present case are clearly analogous. Here also the payment was made in respect of a breach of the law, and it was in no way necessary for the late Rai Bahadur Sardar Narain Singh to incur such expenditure in order to earn his income from fees as a director of the Company. I submit therefore that the answer to the question which has been stated should be in the negative.

Tek Chand, for the Assessee.

Raj Krishna for the Commissioner.

JUDGMENT.

DIN MOHAMMAD, J.—This is a reference under Section 66 (2) made by the Commissioner of Income-tax, at the instance of the executors of the estate of the late Rai Bahadur S. Narain Singh. The question at issue arose in the following circumstances :—

Rai Bahadur Narain Singh was one of the directors of the People's Bank of Northern India, which went into liquidation some time in 1935, and was placed in charge of an official liquidator. In the course of the liquidation proceedings it was suspected that the directors of the Bank had been guilty of issuing false balance-sheets and of otherwise misappropriating the money under their control and consequently it was decided to take action against them under the relevant sections of the Indian Companies Act. Misfeasance proceedings were actually started against Rai Bahadur Narain Singh among others and in the course of those proceedings Rai Bahadur Narain Singh expressed his willingness to pay Rs. 35,000 in order to get rid of them. This offer was accepted. The Rai Bahadur paid the money and the proceedings were dropped. In the return submitted on behalf of the Rai Bahadur for the assessment year 1939-1940, the executors claimed a deduction for this amount. Their claim, however, was rejected by the Income-tax Officer as well as by the Assistant Commissioner on appeal. Thereupon, the executors made a petition to the Commissioner under Section 66 (2) of the Indian Income-tax Act, requiring him to refer to this Court the following question :—

“ Whether in the circumstances of the case, the sum of Rs. 35,000 claimed as a deduction is allowable or not under the provisions of Sections 10 and 12 of the Indian Income-tax Act, 1922.”

The Commissioner has acceded to the request of the executors but has expressed an opinion that the deduction claimed by them is not a permissible deduction.

Counsel for the executors has urged that the deduction falls both under Section 10 (2) (xii) and Section 12 (2) of the Income-tax Act. The relevant provisions may for facility of reference be reproduced below :—

Section 10 (2).—“ Such profits or gains shall be computed after making the following allowances, namely :—

(xii) Any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of such business, profession or vocation.”

Section 12 (2).—“ Such income, profits and gains shall be computed after making allowance for any expenditure (not being in the

nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains."

Counsel for the executors further refers to Section 235 (1) of Indian Companies Act in support of his contention, the material portion of which reads as follows:—

"Where in the course of winding up a company, it appears that of any past or present director has mis-applied any money or property of the company, or been guilty of any misfeasance or breach of trust in relation to the company, the Court may on the application of the liquidator, examine into the conduct of the director and compel him to repay or restore the money or property or any part thereof respectively with interest at such rate as the Court thinks just, or to contribute such sum to the assets of the company by way of compensation in respect of the mis-application, retainer, misfeasance or breach of trust as the Court thinks just."

Counsel for the executors argues that inasmuch as the late Rai Bahadur was called upon by the Court to contribute Rs. 35,000 assets of the bank in the capacity of a director of the Bank, this expenditure was incurred by him for the purpose of this business and could not therefore be computed in the assessable income. I, however, think that apart from all other considerations and independently of all the authorities cited to us, the proposition advanced by the executors cannot be accepted on a strict interpretation of the provisions of law relied upon by them. In the first place, the working of both Sections 10 (2) (xii) and 12 (2) definitely exclude any expenditure in the nature of capital expenditure and counsel has not made any attempt to show that the expenditure incurred by the Rai Bahadur for which this deduction is claimed was not of this nature. All that he stressed was that the sum was not levied as penalty but as contribution to the assets of the company as contemplated in the alternative by Section 235 of the Companies Act. But even if this was so, it does not necessarily lead to the conclusion that it was not in the nature of capital expenditure. A contribution made by a shareholder of a company to its assets will not ordinarily be a permissible deduction. How can this contribution which under the terms of the statute is a contribution to the assets of the company be placed on different footing? Secondly, as I read Section 10, it contemplates profits and gains of a business, profession or vocation carried on by an assessee and subsection (2) of that section enumerates the allowances which are to be made in calculating such profits or gains. Item No. (xii) definitely contemplates that the expenditure to be excluded should have been

"laid out or expended wholly and exclusively for the purpose of such business, profession or vocation." It cannot in any sense of the term be contended by the executors that this sum was so spent for the purpose of the business, profession or vocation in respect of which the return was furnished by the assessee. Similarly sub-section (2) of Section 12 emphasises the fact that the expenditure to be excluded must be one "incurred solely for the purpose of making or earning such income, profits or gains." On the terms of these provisions, therefore, this deduction cannot be claimed. Thirdly, in my view the deduction to be made should relate to the income which is included in the return as in both the provisions relied upon the words "income, profits and gains" are qualified by the word "such" and this evidently means that the income, profits or gains from which a deduction is to be made are those which are shown as taxable in the return in which the deduction is claimed.

Counsel for the executors referred to an unreported English case in which a solicitor had been allowed to deduct the loss incurred by him in compensating his client for neglecting to perform his duty towards him in a proper manner. He further relied on footnote (q) appended to paragraph 4 at page 112 of *Pratt and Redman's Income-tax Law*. None of these authorities, however, is in point. In fact, if properly scrutinised the cases relied on go against the executors. A loss incurred in a business may be lawfully deducted but by no stretch of language can the sum under discussion be described as a loss.

Counsel for the Commissioner places his reliance on the principles deducible from *Commissioners of Inland Revenue v. Alexander Von Glehn & Co., Ltd.*¹, *In re Amrita Bazar Patrika*², *Kangra Valley Slate Company, Ltd. v. Commissioner of Income-tax, Punjab*³, *Lachmi Narain Gadodia and Co. v. Commissioner of Income-tax, Punjab*⁴, *Ramaswami Chettiar and Others v. Commissioner of Income-tax*⁵ and *Commissioner of Income-tax, Burma v. Gasper and Company, Rangoon*⁶. I consider that though these judgments too do not directly touch the matter now before us, their *ratio decidendi* can be safely relied upon in disposing of this matter.

I would, therefore, hold that the deduction claimed is not permissible and answer the question put to us accordingly. I would further allow full costs of this reference to the Commissioner.

SALE, J.—I agree.

Reference answered accordingly.

(1) '1920) 12 Tax Cas. 232.

(2) (1937) 5 I.T.R. 648.

(3) (1935) 3 I.T.R. 324; I.L.R. 16 Lah. 479.

(4) (1934) 2 I.T.R. 322; I.L.R. 16 Lah. 494.

(5) (1930) A.I.R. 1930 Mad. 808.

(6) (1940) 8 I.T.R. 100.

[IN THE MADRAS HIGH COURT.]

C. K. MAMAD KEYI

v.

COMMISSIONER OF INCOME-TAX, MADRAS.

SIR LIONEL LEACH, C.J., and LAKSHMANA RAO, J.

August 20, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 9 (1) (iv) AND (v)—INCOME FROM PROPERTY—ALLOWANCES—URBAN IMMOVABLE PROPERTY TAX LEVIED UNDER BOMBAY FINANCE ACT, 1932—WHETHER AN 'ANNUAL CHARGE'—WHETHER 'LAND REVENUE'—BOMBAY FINANCE ACT, 1932, SEC. 24-B—BOMBAY FINANCE (AMENDMENT) ACT, 1939—BOMBAY FINANCE (SECOND AMENDMENT) ACT, 1939.

The urban immovable property tax levied on immovable property situated in the City of Bombay under the Bombay Finance Act, 1932, as amended by the Bombay Finance (Amendment) Act, 1939, and which by Section 24-B of that Act, introduced by the Bombay Finance (Second Amendment) Act, 1939, becomes a first charge on the property subject to the prior payment of land revenue, does not come within the expression "an annual charge" in Section 9 (1) (iv) of the Income-tax Act. The tax is in no way different from taxes levied by a municipality and it does not constitute 'land revenue' within the meaning of Section 9 (1) (v) of the Income-tax Act.

Consequently an assessee who owns immovable property in the City of Bombay is not entitled to deduct from his income from property either under Section 9 (1) (iv) or Section 9 (1) (v) of the Income-tax Act the urban immovable property tax levied under the Bombay Finance Act, 1932, as amended by the Bombay Finance (Amendment) Act, 1939.

Cases referred to :—

Commissioner of Income-tax, Bombay v. Mahomedbhoj Rowji [1943] (11 I.T.R. 320).

Dakshina Mohun Roy Chowdhry v. Saroda Mohun Roy Chowdhry [1893] (20 I.A. 160).

Case referred to the Madras High Court by the Income-tax Appellate Tribunal under Section 66 (1) of the Income-tax Act (XI of 1922) as amended by Section 92 of the Income-tax (Amendment) Act (VII of 1939) in Application 66 R. A. No. 11 Madras of 1942-43 on its file for decision on the following question of law, *vis.*, :—

"Whether the sum of Rs. 10,880 (or any portion of it) being Urban Immovable Property Tax paid under the Bombay Finance Act is not an admissible deduction under Section 9 (1) (iv) or 9 (1) (v) in computing the income from property under Section 9 of the Income-tax Act."

Case Referred No. 17 of 1943.

Under Section 38 of the Indian Income-tax Act (XI of 1922) the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. VERMA (Judicial Member) and P. N. S. AIYAR (Accountant Member) delivered the following judgment on 24th July 1942.

JUDGMENT OF THE APPELLATE TRIBUNAL.

“ Three objections have been raised in this appeal and they are :—

(i) Increase by the sum of Rs. 18,000 of the income from property in respect of two items 117 and 118 in the list of schedule of “ properties ” submitted by the appellant ;

(ii) disallowance of the sum of Rs. 10,880 paid as urban property tax in respect of properties in Bombay, claimed as deduction in arriving at the income under the head “ property ” ;

(iii) disallowance of the sum of Rs. 581 scavenging tax, water tax, lighting tax and education tax paid in respect of properties at Cannanore, Tellicherry, Calicut and Mangalore, income of which has been charged under the head income from “ property.”

The appellant has filed an application requesting an enquiry into the matters alleged and it as been placed on the file.

2. The appellant contends that in respect of item 117 the property had been given on six years' lease and the rent was fixed at Rs. 550 per mensem and the increase of this income from this property by Rs. 10,000 as made by the Income-tax Officer on the basis of valuation made by the Bombay Municipality is not warranted. He contends that under the Bombay Municipal Act taxes are levied on the basis of “ rateable value ” of buildings, *vide* Section 140 (a), (b) and (c) of that Act. The term ‘ rateable value ’ has not been defined in the Act but there is a difference in the rateable value and the letting value and he states that the Bombay Municipal Act provides that when the two are different the proportionate tax on the difference will be recoverable by the landlord from the tenant. On this he argues that the adoption of the Bombay ‘ rateable value ’ in respect of this property for arriving at the *bona fide* annual value was not justified. We find this contention of the appellant has not been considered by either of the officers below. With regard to item 118 the appellant contends that the annual rental value was Rs. 300 per year or Rs. 25 per month which he has given in the schedule, that the building on that land belonged to the sub-lessee and the income from that property does not belong to him and therefore the assessment by the Income-tax Officer of the sum of Rs. 8,000 on this account was not warranted. We find this contention of the appellant goes to the very root of the assessment but this has not been considered either by the Income-tax Officer or the Appellate Assistant

Commissioner. We, therefore, cancel this portion of the assessment order and direct the Income-tax Officer to examine the contention of the appellant in respect of these two objections and dispose of it according to law.

3. As regards the second objection regarding the disallowance of urban property tax paid, we are unable to accept the appellant's contention that it is an admissible deduction. We do not find this item included in the list of deductions mentioned in the section itself. He contends that this is in the nature of land revenue and when payment of land revenue is allowed, deduction of this should also be allowed. This is a tax levied by the Bombay Government under the Finance Act and it is a tax on land and building based on the rateable value and is therefore not an admissible deduction under the Income-tax Act.

4. The next contention as regards this disallowance of Rs. 581 scavenging tax, water tax, lighting tax and education tax paid in respect of properties in Madras Presidency, the Income-tax Officer declined to allow on the ground that under the Madras Municipal Act these amounts are payable by the owner and not by the occupier. The appellant contends that these are occupier's burden borne by the owner and are to be considered in arriving at the *bona fide* annual value. This aspect of the matter it would appear has not been considered by the Income-tax Officer. His order in respect of this disallowance is set aside and he is directed to enquire into this claim of the appellant that it is the occupier's burden borne by him and if that is found to be so, the appellant will be entitled to the deduction.

5. The result is the appeal is partially allowed and the Income-tax Officer is directed to make a fresh enquiry in regard to the items mentioned in the order."

On the application of the assessee under Section 66 (1) of the Indian Income-tax Act (XI of 1922), the Appellate Tribunal referred the case to the Madras High Court.

STATEMENT OF CASE.

" The applicant seeks reference of the following question of law said to arise from the order of this Bench of the Tribunal dated the 24th July 1942, to the High Court of Judicature at Madras :—

" Whether the whole or any portion of Rs. 10,880 paid by the assessee to the Bombay Government under the Finance Act as amended by Section 7 of Act IV of 1939 and Act I of 1940 is not a permissible deduction under the Income-tax Act ? "

2. The Commissioner of Income-tax, Madras, who is the respondent to this application has submitted his reply under Rule 54 of the

Tribunal Rules and has stated that the question that arises out of the order of this Bench of the Tribunal is as under :—

“Whether the sum of Rs. 10,880 (or any portion of it) being Urban Immovable Property tax paid under the Bombay Finance Act is not an admissible deduction under Section 9 (1) (iv) or 9 (1) (v) in computing the income from property under Section 9 of the Act?”

The respondent has further challenged certain statement of facts as being incorrect. The reply of the Commissioner is made a part of the record to be submitted to the High Court. The question to be referred hereafter being one of law we proceed to state the case.

3. The question raised can be stated in a small compass as it concerns merely one item regarding the imposition of tax called the Urban Immovable Property Tax under the Bombay Finance Act, 1939. It was contended before us that the Bombay Urban Immovable Property Tax is an admissible deduction under Section 9 of the Indian Income-tax Act. This Bench of the Tribunal however, did not agree with the contention of the applicant. Admissible deductions are mentioned in Section 9 of the Indian Income-tax Act. Anything beyond that is not an admissible deduction.

4. The point raised was that the tax paid is in the nature of the land revenue and that it should have been allowed under the category of land revenue allowable under Section 9 (1) (iv) or in any case under Section 9 (1) (v) of the Indian Income-tax Act. It was common ground before us that the tax is levied by the Bombay Government under its Finance Act and that the amount of the tax is determined both on the land and the building based on the rateable value. The land revenue may be defined as the revenue derived by State by taxation of land and of profits from lands. Generally land revenue is assessed on agricultural land (?) Provincial Acts as it is revenue of State purely on land. In the case before us it is not the land, the value of which is estimated for Urban Property Tax Act but as the name itself indicates it is on account of the property in the urban area. It is the nature and valuation of property that determines the tax and not the land on which it stands.

5. It appears clearly that this was not tax on land nor can the imposition be called land revenue. What the Government has to take into consideration in arriving at the value is the letting value of the building inclusive of the land on which it stands and not the land alone. This Bench of the Tribunal accordingly considered that it is not land revenue and as such it is not an admissible deduction.

6. This Bench of the Tribunal, however, has not considered the amount of the valuation of the tax whether it represented correctly the figure but only ruled against the appellant on the question of law raised.

7. The question therefore which is raised and which is one purely of law is referred to the High Court in the following form:—

Question of law referred.—"Whether the sum of Rs. 1,880 (or any portion of it) being Urban Immovable Property Tax paid under the Bombay Finance Act is not an admissible deduction under Section 9 (1) (iv) or 9 (1) (v) in computing the income from property under Section 9 of the Income-tax Act?"

8. The papers mentioned in the Index attached will form the paper book in this case."

M. Subbaraya Ayyar, for the assessee.

K. V. Sesha Ayyangar, for the Commissioner.

JUDGMENT.

(Judgment of the Court was delivered by the Hon'ble the Chief Justice).

The assessee who is a resident of Tellichery owns immovable property of considerable value in the City of Bombay. In respect of the financial year 1940-41 he contended that he was entitled to deduct, when calculating his income assessable under Section 9 of the Income-tax Act, the sum of Rs. 10,880 which he had been compelled to pay by the Government of Bombay as urban immovable property tax on his properties within the City of Bombay. The Income-tax authorities rejected his contention and the Appellate Tribunal, Calcutta Bench, held that they were right. Thereupon the assessee asked the Tribunal to state a case to this Court under Section 66 (1). The Tribunal acceded to this request and the question referred is in these words:—

"Whether the sum of Rs. 10,880 (or any portion of it) being Urban Immovable Property Tax paid under the Bombay Finance Act is not an admissible deduction under Section 9 (1) (iv) or 9 (1) (v) in computing the income from property under Section 9 of the Income-tax Act?"

Sub-section (1) of Section 9 says that the tax shall be payable by an assessee under the head "Income from property" in respect of the *bona fide* annual value of property consisting of buildings or lands appurtenant thereto of which he is the owner, other than such portions of the property as he may occupy for the purpose of his business, profession or vocation. The sub-section proceeds to set out what deductions can be made. Clause (iv) of sub-section (1) allows *inter alia* a deduction where the property is subject to an annual charge not being a capital charge, the deduction being the amount of the charge. Clause (v) allows an assessee to deduct any sums paid "on account of land revenue." The assessee says that he is entitled to make the deduction under one or other of these clauses.

The Bombay Finance (Amendment) Act, 1939, added a new chapter to the Bombay Finance Act, 1932. The new chapter contains a provision with regard to the imposition of the urban immovable property tax on lands and buildings in the City of Bombay and in other parts of the Bombay Presidency. The tax in the City of Bombay is 5 per cent. on the annual letting value. By the Bombay Finance (Second Amendment) Act, 1939, certain further amendments were made in the Act of 1932. One of these amendments was the insertion of Section 24-B in the chapter relating to the urban immovable property tax. This section reads as follows:—

“Notwithstanding anything contained in any law and notwithstanding any rights arising out of any contract or otherwise howsoever, all sums due on account of the Urban Immovable Property Tax levied under Section 22 or as a penalty imposed under Section 24-A for failure to pay such tax, in respect of any building or land, shall, subject to the prior payment of the land revenue, if any, due to the Provincial Government thereon, be a first charge upon the said building or land and upon the movable property, if any, found within or upon such building or land and belonging to the person liable for such tax or penalty.”

In the first place the assessee says that as a charge is created by this section he is entitled to the deduction under clause (iv) of subsection (1) of Section 9 of the Income-tax Act. To accept this contention would mean that municipal taxes are deductible under this clause because the amounts due in respect of municipal taxes levied are likewise made a charge on the property. Municipal taxes are not deductible under Section 9 and Mr. M. Subbaraya Ayyar, on behalf of the assessee has accepted this. In a recent case heard by the Bombay High Court it was suggested that the municipal taxes represent an annual charge upon the property within the meaning of Section 9 (1) (iv), but this contention was rejected. See *Commissioner of Income-tax, Bombay v. Mahomedbhoy Rowji*¹. Section 24-B of the Bombay Finance Act, 1932, does not create “an annual charge” upon the property. It operates to create a charge should the owner of the property fail to pay the urban immovable property tax. That is not an annual charge within the meaning of Section 9 of the Income-tax Act. There is no substance in the first contention.

The second contention, that based on clause (v) is perhaps more arguable, but here again we consider that the proper view was taken by the Appellate Tribunal. The term “land revenue” is not defined in the Income-tax Act, or, as far as we are aware, in any other statute. In *Dakshina Mohun Roy Chowdhry v. Saroda Mohun Roy Chowdhry*²,

(1) (1943) 11 I.T.R. 320.

(2) 20 I.A. 160.

Lord Macnaghten in delivering the judgment of the Privy Council observed :

“ The Government revenue represents that portion of the produce of the land which from time immemorial has been considered in eastern countries to belong as of right to the sovereign power in the State. In India payment in kind has long since been commuted for a money payment, which in some cases is fixed permanently and in others is liable to revision by periodical settlements. Sometimes the Government revenue is spoken of as quit-rent, sometimes as a land tax. But, however it may be described and however it may have been assessed, it is the first and paramount charge upon the land, and if default is made in payment the estate is sold in a summary way.”

The Legislature of the Bombay Presidency clearly does not regard the urban immovable property tax as constituting “ land revenue.” This is shown by Section 24-B which makes the charge subject to the prior payment of the land revenue, if any, due to the Government. Mr. Subbaraya Ayyar has contended however, that we should ignore what is said in Section 24-B because in the City of Bombay lands are held in freehold and part of the tax must be allocated to the land. A tax on land must, he says, be regarded as being land revenue. He admits that this argument will not apply to lands held outside the City of Bombay, because such lands already pay revenue to Government. We cannot accept this argument. If the tax does not constitute “ land revenue ” within the meaning of Section 9 (1) (v) of the Income-tax Act in respect of lands outside the City of Bombay it does not constitute land revenue within the City. In our opinion the urban immovable property tax of the Bombay Presidency is in no way different so far as the Income-tax Act is concerned from taxes levied by a municipality. Moreover the Bombay Act itself distinguishes it from “ land revenue.”

For these reasons the answer to the reference is that the assessee is not entitled to any deduction. The assessee must pay the costs of the reference Rs. 250.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

LAKSHMI NARAIN GADODIA & CO., *In re*

DIN MOHAMMAD and SALE, JJ.

May 18, 1948.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 8, 34, 66 (3)—STATUS OF ASSESSEE—INDIVIDUAL OR HINDU UNDIVIDED FAMILY—SELF-ACQUIRED PROPERTY—ASSESSMENT AS INDIVIDUAL FOR SEVERAL YEARS—ADOPTED SON SUBSEQUENTLY TAKEN INTO BUSINESS—STATEMENT THAT BUSINESS BELONGS TO JOINT FAMILY AND ASSESSMENT ACCORDINGLY—NOTICE UNDER SEC. 34 FOR RE-ASSESSMENT AS INDIVIDUAL—LEGALITY—VALUE OF AFFIDAVIT—STATUS—QUESTION OF FACT—JURISDICTION OF HIGH COURT.

The assessee who was carrying on business in partnership with another, separated from the latter in 1934 and took his adopted son into the business and the son began to work with him. The business of the assessee being self-acquired, he was assessed up to 1935-36 in his individual capacity both for income-tax and super-tax. In 1936-37 he was assessed for the first time as a Hindu undivided family consisting of himself and his adopted son. In 1937-38 the Income-tax Officer examined him on the question of status and accepted his contention that the assessment should be made on him as a Hindu undivided family in view of the adoption of a son. On 22nd February 1938, the Income-tax Officer decided that the status of the assessee should be that of an individual and issued a notice under Section 34 to revise the super-tax assessment for 1937-38. In response to this notice the assessee made a return as a member of a Hindu undivided family and filed an affidavit to the effect that all the property of the firm was the property of a joint Hindu family consisting of himself and his adopted son.

Held, (i) that Section 34 gives power to the Income-tax authorities to take action, where, *inter alia*, the assessee "has been assessed at too low a rate or has been the subject of an excessive relief under the Act" and that therefore under the circumstances of the case the Income-tax Officer was empowered to use Section 34;

(ii) that the question of status would normally be a question of fact and the High Court would have no jurisdiction to interfere with the finding of the Income-tax authorities arrived at on a proper appreciation of the facts, but in arriving at this finding they should not misappreciate the law bearing on the subject;

(iii) that as a clear intention to waive the separate rights of the assessee to the properties was established by the affidavit, the Income-tax

authorities should have found that the properties belonged to a joint Hindu family.

OBITER.—*The jurisdiction of the High Court under Section 66 (3) is confined to those matters which are contained in the application made to the Commissioner under Section 66 (2) and it is only in relation to such matters that the refusal of the Commissioner to state a case can subsequently be investigated.*

Cases referred to ;—

Raj Kishore v. Madan Gopal (1932) 13 Lah. 491 ; 143 I.C. 249.

Som Chand Maluk Chand v. Commissioner of Income-tax (1938) 6 I.T.R. 297 ; 1938 Lah. 477 ; 177 I.C. 222 ; 40 P.L.R. 308 ; A.I.R. 1938 Lah. 545.

Case stated under Section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Punjab : (Civil Reference Case No. 6 of 1941).

STATEMENT OF CASE.

"Facts of the case.—Seth Lakshmi Narain Gadodia (hereinafter called the assessee) is a Hindu governed by the Mitakshara Law. The family originally belonged to Bhiwani in the Hissar District where they owned a residential house worth about Rs. 5,000. It is admitted that this is the only ancestral property and that there is no ancestral business. The assessee moved to Delhi about fifty years ago and obtained employment with a Delhi firm. Later he entered into partnership with a firm styled Gowardhan Das-Ram Gopal and after some time he started another business under the name of L. N. Gadodia & Co., in partnership with a certain Benarsi Das. This partnership was dissolved in 1934. Since then the assessee has been carrying on the business under the same name without any outside partner. It is admitted that apart from the ancestral property at Bhiwani the whole of his present income is self-acquired. He had only one child (a daughter) who is now married. In or about the year 1924 he adopted a boy named Ram Gopal as his son and this adopted son is now about 21 years old. He was removed from college at about the age of 15 and since then he has been working in his adoptive father's business.

Up to the year 1935-36 all assessments were made on Seth Lakshmi Narain Gadodia as an individual, and he appears to have raised no objection to this procedure. The assessment order for 1936-37 again shows the status as "individual" but the Income-tax Officer, without recording any finding on the subject, treated the income as the income of a Hindu undivided family for the purpose of super-tax, allowing exemption on the first Rs. 75,000 instead of the first Rs. 30,000. In 1937-38 the Income-tax Officer examined the assessee on this point and

accepted his contention that the assessment should be made in the status of a Hindu undivided family in view of the adoption of a son. Subsequently, however, it was realised that this fact alone was not sufficient to convert the income derived from the assessee's self-acquired property into the income of a joint family. A notice was, therefore, issued under Section 34. The assessee then claimed that he had thrown his self-acquired property into the common stock, but the Income-tax Officer did not accept this contention and made a supplementary assessment by which he imposed super-tax on the excess of over Rs. 80,000. This decision was confirmed by the Assistant Commissioner on appeal. Copies of the assessment and appellate orders are appended as Exhibits 'A' and 'B'. The assessee then submitted an application under Section 66 (2) but my predecessor refused to interfere with the assessment or to make a reference to the High Court. Copies of the application and of my predecessor's order are appended as Exhibits 'C' and 'D'.

Questions for consideration.—As a result of a subsequent petition under Section 66 (3) I have been required to refer the following questions of law :—

(1) Is the notice under Section 34 justified in the circumstances of this case?

(2) Has all the evidence on the record been considered in arriving at the finding whether the assessee has or has not divested himself of the self-acquired property and the property belongs now to the joint Hindu family?

Opinion of the Commissioner.—As regards the first question I venture to point out that in his application under Section 66 (2) the assessee did not dispute the validity of the supplementary assessment and this point was therefore not discussed in the order passed by my predecessor. In the case of *Som Chund-Maluk Chand v. Commissioner of Income-tax, Punjab*¹, it was held that the jurisdiction of the High Court under Section 66 (3) is confined to those matters which are contained in the application made to the Commissioner under Section 66 (2) and that it is only in relation to such matters that the refusal of the Commissioner to state a case can subsequently be investigated. If, however, your Lordships are disposed to consider the question I would respectfully invite a reference to the decision of the Bombay High Court in *Commissioner of Income-tax, Bombay v. D. R. Naik*² where it was held in exactly similar circumstances that the Income-tax Officer was entitled to take action under Section 34 with a view to reducing the super-tax exemption which had previously been allowed.

(1) (1938) 6 I.T.R. 297.

(2) (1939) 7 I.T.R. 362.

As regards the second question it is an accepted principle of Hindu Law (*Mulla's Hindu Law*, 9th edition, page 246) that where a member of a joint family claims to have thrown his self-acquired property into the common stock a clear intention to waive his separate rights must be established, and such intention cannot be inferred from the mere fact of his allowing the other members of the family to use it conjointly with himself. Since the mandamus order was received I have given the assessee a further opportunity of explaining the evidence on which he bases his claim that this was in fact his intention. The material now available on the records may be summarised as follows :—

(1) The assessee produced before the Income-tax Officer an affidavit, dated the 12th of April, 1938, to the effect that his adopted son, his wife and himself constituted a joint Hindu family and that all the property originally owned and acquired by him had been voluntarily thrown into the common stock. This affidavit was only filed after the receipt of the notice under Section 34 which was issued on the 22nd of February, 1938, and as my predecessor has pointed out in his order it is not of much value in view of the provisions of Section 54 of the Income-tax Act. As the affidavit forms a part of the confidential records of the Income-tax Department it is not accessible to the general public and cannot therefore be used against the assessee. There is no evidence that he has made any public declaration to the same effect.

(2) In the year 1928, about four years after the adoption, the assessee transferred a sum of Rs. 1,00,000 to a trust whose income was to be used for educational and other charitable purposes. Under the terms of the trust deed his adopted son is to become a trustee after his death, but this provision does not necessarily imply that the rest of his self-acquired property is joint. Indeed the fact that the trust was created indicates that the assessee still regarded his property as belonging to himself individually.

(3) In 1933 certain property was acquired in the joint names of the assessee and his adopted son, and about the same time certain other property was acquired in the name of the son alone. When the Income-tax Officer asked for the account books of that year he was told that they had been destroyed. He found, however, from subsequent accounts that expenses amounting to Rs. 40,000 which had been spent on protracted litigation in connection with the same property had at first been debited to "Gharkharch" or household expenses but had later been adjusted in the personal account of the assessee. The rental income of the property had also been adjusted in his personal account.

If the assessee had consistently made all purchases in the joint names, or in his own name as *karta* of the family, and had adjusted all payments in joint accounts, that would certainly have supported his present contention, but it is clear that he has not in fact adopted a consistent procedure of this kind, and the accounts which he has made available seem rather to indicate that he still regards the assets in question as his personal property.

(4) On the 17th December, 1938, the assessee intimated to the various banks with which he had dealings that "my son Ram Gopal has become a major and is authorised to operate the accounts." This, however, is a letter which might well have been written with regard to a new partner or manager of a business, and does not necessarily imply that the assets are jointly owned. There is no evidence of the opening of any joint family account as distinct from the private accounts in the name of the assessee himself.

(5) In the invitations sent out in connection with the wedding of Ram Gopal which was celebrated in December, 1939, the assessee and his wife described him as "their son." This fact might help to establish the genuineness of the adoption, if that were in dispute, but it is scarcely relevant to the question of the ownership of the assets.

For the above reasons I submit that the evidence has been duly considered, and that it is not sufficient to establish a definite intention to waive separate rights in the property.

I am, therefore, of opinion that both questions should be answered in the affirmative."

M. C. Mahajan, A. R. Kapur and Bhagwat Dayal, for the assessee.
Raj Krishna, for the Commissioner.

JUDGMENT.

SALE, J.—This is a case stated by the Income-tax Commissioner, in response to a mandamus by a Bench of this Court on a petition by Seth Lakshmi Narain Gadodia, assessee, who carried on business in Delhi under the name of L. N. Gadodia & Co. The assessment in question is for the year 1937-38. The material facts are that Seth Lakshmi Narain Gadodia started business in Delhi many years ago, in a partnership styled Gowardhan Das Ram Gopal. Later, the name of the firm was changed to L. N. Gadodia & Co., and until 1934 was carried on in partnership with one Benarsi Das. This partnership was dissolved in 1934. Since then Seth Lakshmi Narain Gadodia has been carrying on business under the same name without any outside partner. Apart from the possession of an ancestral house at Bhiwani (which is immaterial for the purposes of this reference) the whole of the

property relating to the Delhi firm is self-acquired. In or about the year 1924 Seth Lakshmi Narain Gadodia adopted a son named Ram Gopal, then aged about 5. The education of this boy ceased in 1934, when Seth Lakshmi Narain Gadodia took this boy then aged about 15 into his business, since when he has been working in his adoptive father's business.

Up till 1935-36 Seth Lakshmi Narain Gadodia was assessed in his individual capacity both for income-tax and super-tax. In 1936-37 he was for the first time assessed as a Hindu undivided family, for 1937-38, by an order dated 29th November 1937, a definite finding was recorded by the Income-tax Officer that he was a *karta* of an undivided Hindu family and he was again assessed accordingly. The undivided family in question according to the petitioner consisted of himself and his adopted son Ram Gopal.

But on the 22nd of February 1938, the same Income-tax Officer issued a notice under Section 34 of the Income-tax Act to revise the assessment for 1937-38. On 26th March 1938 the assessee made a return in response to this notice as a member of a Hindu undivided family and in this connection on 12th April 1938 he filed an affidavit to the effect that all the property of the firm was the property of a joint Hindu family consisting of himself and his adopted son. Nevertheless, on 21st May 1938 the successor of the Income-tax Officer who had issued the notice under Section 34 decided that the status of the assessee should be that of an individual and assessed him accordingly. The effect of this change of status was that Seth Lakshmi Narain Gadodia was assessed to increased super-tax. An appeal against this order was dismissed by the Assistant Commissioner of Income-tax on 30th September 1938. A reference to the High Court was refused whereupon the assessee petitioned this Court, and a Bench accepted the petition directing the Commissioner of Income-tax to state a case on two questions which were formulated as follows :—

“(1) Is the notice under Section 34 justified in the circumstances of this case ?

(2) Has all the evidence on the record been considered in arriving at the finding whether the assessee has or has not divested himself of the self-acquired property and the property belongs now to the joint Hindu family ?”

During the hearing of petition which gave rise to this mandamus it was argued that Section 34 has been misapplied on the ground that there was no “escape” of income from assessment. In arguments before us Mr. Mehr Chand Mahajan has urged that Section 34 cannot be used to revise a finding regarding the status of an assessee.

The Commissioner has correctly pointed out in his statement that in his application under Section 66 (2) the assessee did not dispute the applicability of Section 34 for the purpose of making a supplementary assessment and he referred to *Som Chand Maluk Chand v. Commissioner of Income-tax*¹ in which a Division Bench of this Court of which one of us was a member, held that the jurisdiction of the High Court under Section 66 (3) is confined to those matters which are contained in the application made to the Commissioner under Section 66 (2) and that it is only in relation to such matters that the refusal of the Commissioner to state a case can subsequently be investigated. In the present case, however, no objection on this score was raised by counsel for the Commissioner of Income-tax when the mandamus petition was argued and although I have no doubt that the ruling referred to lays down the correct law, I consider that in the circumstances of this case the petitioner is entitled to argue the question as propounded by the mandamus Bench as to whether the notice under Section 34 was justified in the circumstances of this case.

In point of fact, the question of "escape" from assessment does not arise in this case; and it is unnecessary, therefore, to consider the somewhat controversial point of the proper interpretation of the word "escape" as used in Section 34. In the present case the sole question involved was assessment of income for the purpose of super-tax. The acceptance of the status of the assessee as that of a joint Hindu family had led to a high exemption being granted to the assessee for the purpose of assessment of super-tax; and it was because the assessee was held by the Income-tax Officer to have been assessed at too low a figure for this purpose, that the notice under Section 34 was issued. Section 34 gives power to the Income-tax authorities to take action where, *inter alia*, the assessee "has been assessed at too low a rate or has been the subject of an excessive relief under the Act." There can be no question, therefore, that the Income-tax Officer was empowered to use Section 34 in the circumstances of this case and I would, therefore, answer in the affirmative the first question whether notice under Section 34 was justified in the circumstances of this case.

Turning now to the second question, it has to be noted that the Commissioner of Income-tax in his statement in response to the mandamus, has mentioned that in connection with the 1937-38 assessment, the Income-tax Officer examined the assessee on the question of status "and accepted his contention that the assessment should be made in the status of a Hindu undivided family in view of the adoption of a son." The records before us do not include any statement by the assessee or

a separate finding of the Income-tax Officer on this point. But we have been informed that some of the records of this case, were burnt in the Delhi disturbances of 1942, and in the circumstances I see no reason why the statement of the Commissioner of Income-tax on this point should not be accepted, especially as the fact is confirmed by the affidavit (which is on the record) made by the assessee on 12th April 1938 following the notice under Section 34. In this affidavit the assessee has asserted that he has thrown all his property into the common stock and that the business now belongs to a joint Hindu family consisting of himself and his minor son. This affidavit relates not only to the future intention of the assessee but also recites acts which he has done in the past, in furtherance of this intention.

Now the question of status would normally, as pointed out in the mandamus order, be one of fact and if the Income-tax authorities had held on a proper appreciation of the facts that the status of the assessee should be that of an individual, this Court would have no jurisdiction to interfere. But it appears to me that in coming to this decision the Income-tax authorities have misappreciated the law bearing on the subject. The Commissioner of Income-tax rightly refers to *Mulla's Hindu Law*, Section 227, printed on page 246 of the 9th edition where it is laid down that "property, which was originally the separate or self-acquired property of a member of a joint family, may become joint family property, if it has been voluntarily thrown by him into the common stock with the intention of abandoning all separate claims upon it. A clear intention to waive his separate rights must be established." (Reference may be made in this connection to a Division Bench judgment of this Court, *Raj Kishore v. Madan Gopal*¹). But where I consider the learned Income-tax Commissioner has gone wrong in law is in refusing to accept the declaration by the assessee as evidence of his intention, in the absence of any evidence to show that the declaration was bogus or otherwise unreliable. In referring to the material available on the record the learned Income-tax Commissioner has said that the affidavit under Section 34 "is not of much value in view of the provisions of Section 54 of the Income-tax Act. As the affidavit forms a part of the confidential records of the Income-tax Department it is not accessible to the general public and cannot therefore be used against the assessee. There is no evidence that he has made any public declaration to the same effect." This appears to me to be a misconception of the value of the affidavit. Though the affidavit was a part of the confidential records of the Income-tax Department and may not be accessible to the general

(1) (1932) I.L.R. 13 Lah. 491.

public, there is no bar to the use of this affidavit by the parties concerned, nor is any public declaration to the same effect necessary. The affidavit is in fact a declaration on which the assessee can rely.

Other material, which it is argued by Mr. Mehr Chand Mahajan has been overlooked, is the fact that in 1934 the assessee separated from the firm of partners and took over the business himself. Having removed his adopted son from school, he took him into the business since when the son has been taking an active share in the business. Again we must accept the fact that the assessee made a statement before the Income-tax Officer, Mr. Sangat Rai, in connection with the 1937-38 assessment that he had thrown all property into the common stock. From these facts, a clear intention to waive his separate right, is established; and in Hindu Law this is all that is necessary for a finding that the status of the assessee is now that of a joint Hindu family.

I would, therefore, answer the second question by saying that on the material on the record the Income-tax authorities should have found that for the year in question the property belonged to a Hindu undivided family and that for the purposes of assessment for that year, the status of the assessee was that of a Hindu undivided family.

I would, therefore, accept this petition; and since the petitioner has succeeded on the main point, I would in answering this second question in the affirmative hold that the petitioner is entitled to his costs.

DIN MOHAMMAD, J.—I agree. *Reference answered accordingly.*

[IN THE CALCUTTA HIGH COURT.]

COMMISSIONER OF INCOME-TAX, BENGAL

v.

MESSRS. GURUPADA DUTTA AND OTHERS.

DERBYSHIRE, C.J., and GENTLE, J.

June 10, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (xii), SEC. 10 (4)
—PROFITS FROM BUSINESS—ALLOWANCES—RATE IMPOSED UNDER
BENGAL VILLAGE SELF-GOVERNMENT ACT, 1919—WHETHER ALLOW-
ABLE DEDUCTION.

The rate imposed under the provisions of the Bengal Village Self-Government Act, 1919, on a person occupying a building within the Union and using the same for the purpose of business is an allowable deduction in computing the profits of the business under Section 10 of the Indian Income-tax Act.

Case stated to the High Court under Section 66 (1) of the Indian Income-tax Act (XI of 1922), as amended by the Indian Income-tax (Amendment) Act, 1939, by the Income-tax Appellate Tribunal, Calcutta Bench, for the decision of the question mentioned in Para. 1 of the Statement of Case : Special Jurisdiction (Income-tax) : No. 6 of 1942.

Under Section 33 of the Income-tax Act the Tribunal held that the tax was paid to the Union Board for doing business in the premises within their jurisdiction and it was paid for the use of the premises as a business place. The payment was made for the purpose of the business and it was therefore an allowable deduction.

On the application of the Commissioner of Income-tax, Bengal, under Section 66 (1), the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. VERMA (Judicial Member) and P. N. S. AIYAR (Accountant Member) referred the case to the Calcutta High Court on 26th March, 1942.

STATEMENT OF CASE.

"The Commissioner of Income-tax, Bengal, by his petition dated the 11th February 1942, has asked us to refer to the High Court the following question of law as arising out of the order of the Appellate Tribunal in appeal R. A. A. No. 10 of Bengal of 1941-42 :

"Whether the rate imposed under the provisions of the Bengal Village Self-Government Act, 1919, on a person occupying a building within the Union and using the same for the purpose of business is an allowable deduction in computing the profits of the business under Section 10 of the Indian Income-tax Act."

2. The respondent was required by the rules of the Tribunal to file his reply to the application. He has filed his reply and he objects to the reference on the ground that the question of law formulated does not arise. In the arguments addressed to us at the time of hearing, the counsel appearing for the respondent tried only to justify our order on the ground that the order is legally right. The counsel failed to show why the question formulated is not a question of law.

3. The question formulated is so obviously legal that we did not consider it necessary to hear the applicant under Rule 52 of the Tribunal Rules and a notice was issued to the respondent to file his objection, if any.

4. By an order dated the 9th December 1941 this Bench of the Income-tax Appellate Tribunal decided that the sum of Rs. 84 claimed as an expense by the assessee was an allowable deduction in computing the profits. The necessary facts in connection with this allowance may be mentioned :

5. The respondent carries on business at Nalhati where there is levied a Union Board tax. The Income-tax Officer merely disallowed the claim of Rs. 84 claimed by the respondent paid for the Union Board tax without recording any reason. The Appellate Assistant Commissioner, however, dealt with this matter in his order dated the 12th February 1941 and he mentioned that the claim made is not to be allowed as this is a tax on profits. He considered that the tax has been rightly disallowed by the Income-tax Officer.

6. This Bench of the Income-tax Appellate Tribunal took the view that the tax paid to the Union Board for occupying the business premises is an allowable deduction. The reason stated by the Tribunal was that the tax paid to the Union Board is for occupying the business premises and for doing business in the premises within the jurisdiction of the Union. The payment was considered to be for the purpose of the business.

7. Section 37 of the Bengal Village Self-Government Act of 1919, Local Self-Government Department (Government of Bengal Union Board Manual, Vol. I) deals with the imposition of the Union rate and authorises the Union Board to impose yearly on persons who are owners or occupiers or owners and occupiers of buildings, within the Union a rate stated therein. It reads as under :—

“The Union Board shall impose yearly on persons who are owners or occupiers or owners and occupiers of buildings within the Union, a rate amounting to—

(a) the sum required, after deduction of the contribution, if any, made by the Lord Government in this behalf, for the salaries and equipment of the Defadars and Chaukidars and the salaries of the establishment of the Union Board, and

(b) the sum estimated to be required to meet the expenses of the Board in carrying out any of the other purposes of this Act, if such estimate has been approved by more than half the total number of the members of the Board at a meeting specially convened for the purpose, together with ten per cent. above such sums to meet the expenses of collections and the losses due to non-realisation of the rate from defaulters.”

8. Section 38 then deals with the nature of assessment.

It mentions :—

“the rate to be imposed by a Union Board under Section 37 shall be an assessment according to the circumstances within the Union and property within the Union, if any, of the persons liable to the same.”

9. Under Section 101 of the same Act the Local Government was empowered to make rules to carry out the purposes of the said Act,

Rules 1, 2 and 3 of the rules made in pursuance of the powers noted in the Local Government regarding the assessment and collection of the Union rate read as follows :—

1. (1) After preparing the annual budget estimate in Account Form No. 11 and not less than two months and a half before the first day of the year to which the budget relates, the Union Board at a meeting shall proceed to assess the Union rate provided in the estimate according to the circumstances and the property within the Union of the persons liable to assessment :

Provided that the said period may, for reasons to be recorded in writing, be at any time altered by the District Magistrate.

(2) When a Union Board is for the first time constituted in any Union it may assess the Union rate for a portion of the year in which it is so constituted or of the year next following.

2. The Union Board shall first prepare, village by village and in Form No. 1 a list of all persons owning or occupying buildings, whether with or without land appertaining thereto, in the Union, either permanently or temporarily, showing their trade business, etc., within the Union, and the estimated annual income which they derive from buildings or other property or business within the Union. All such persons shall be included in the list even if some are subsequently exempted.

(3) The Board shall, after considering his debts and liabilities, if any, determine the total assessable income of the person concerned, i.e., the income which he derives from business conducted, or from buildings or other property held, within the Union.

10. The applicant has relied on Section 10 (4) of the Income-tax Act for the proposition that the sum of Rs. 84 should not be allowed. Section 10 (4) reads as under :—

“Nothing in clause (ix) or clause (xii) of sub-section (2) shall be deemed to authorise the allowance of any sum paid on account of any cess, rate or tax levied on the profits or gains of any business, profession or vocation or assessed at a proportion of or otherwise on the basis of any such profits or gains ; and nothing in clause (xii) of sub-section (2) shall be deemed to authorise—

(a) any allowance in respect of a payment which is chargeable under the head ‘salaries’ if it is payable without British India and tax has not been paid thereon nor deducted therefrom under Section 18 ; or

(b) any allowance in respect of a payment by way of interest, salary, commission or remuneration made by a firm to any partner of the firm ; or

(c) any allowance in respect of a payment to a provident or other fund established for the benefit of employees unless the employer

has made effective arrangements to secure that tax shall be deducted at source from any payments made from the fund which are taxable under the head 'Salaries.'"

The allowance would not be admissible if it came within Section 10 (4). If the assessment of the Union Board tax was on the profit earned out of the business it is not to be allowed. In the view we have taken of the matter we held that it is not the tax on the income or on the basis of income but the levy is on the basis of the circumstances and property within the Union. There are several matters to be considered in computing the assessable income of the assessment of the Union Board tax under Section 37 of the Union Board Act. The rules framed under this Act of the Bengal Village Self-Government Act of 1919, deal with the manner of assessment and there are several other circumstances than the income of the business to be taken into consideration in arriving at the amount of tax to be levied on each person. It is not in regard to income alone that the tax is levied. If the person within the Union is in debt and not in good circumstances or has no property he may not be taxed. The tax, therefore, is not based on income from or profit of business but is a tax on circumstances and property and is not, in our opinion covered by Section 10 (4) of the Indian Income-tax Act. The question raised, however, being one of law, we have no hesitation to refer it to the High Court.

11. We, therefore, refer the following question to the High Court of Judicature at Fort William at Calcutta :—

"Whether the rate imposed under the provisions of the Bengal Village Self-Government Act, 1919, on a person occupying a building within the Union and using the same for the purpose of business is an allowable deduction in computing the profits of the business under Section 10 of the Indian Income-tax Act."

12. The papers mentioned in the Index will form part of the reference."

Mr. P. B. Chakravarti, for the Commissioner.

JUDGMENT.

DERBYSHIRE, C. J.—We have had the advantage of hearing *Mr. Chakravarti* argue the case on behalf of the Commissioner of Income-tax against the opinion which has been expressed by the Appellate Tribunal. Notwithstanding that argument I am of the opinion that the opinion expressed by the Appellate Tribunal is the correct one and I agree with the reasons that they have given for that opinion. I do not propose to complicate the matter by adding other reasons.

In my opinion the question asked "Whether the rate imposed under the provisions of the Bengal Village Self-Government Act, 1919,

on a person occupying a building within the Union and using the same for the purpose of business is an allowable deduction in computing the profits of the business under Section 10 of the Indian Income-tax Act " should be answered in the following way—" Yes."

The reference being a matter of public importance the respondent in this matter will be awarded costs to the amount of seven gold mohurs inclusive of all costs.

GENTLE, J.—I agree.

Reference answered accordingly.

[IN THE CALCUTTA HIGH COURT.]

KRISHNA HYDRAULIC PRESS LTD.

v.

COMMISSIONER OF INCOME-TAX, BENGAL.

DERBYSHIRE, C. J., and GENTLE, J.

June 8, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE AMENDMENT), SECS. 26 (2), 34—SUCCESSION—RE-ASSESSMENT—CHANGE OF LAW—PURCHASE OF ALL ASSETS OF A MILL EXCEPT ONE ITEM OF GROSS PROFIT—WHETHER SUCCESSION—SUCCESSION IN MARCH 1938—NOTICE UNDER SECTION 34 FOR ASSESSMENT FOR YEAR 1938-39 ISSUED ON SUCCESSOR IN JUNE 1939—CHANGE OF LAW IN APRIL 1939—APPLICABILITY OF NEW LAW—SCOPE OF SEC. 34.

The assessee company which was incorporated on March 3, 1938, acquired by a sale deed of March 4, 1938, in consideration of the payment of one lac of rupees, all the immovable properties including land, buildings, fixed machineries, and other immovable properties of a mill and press owned by a firm at Benares, together with the goodwill of the business and the right to use their name and the benefit of all their contracts and all legal incidents. On June 10, 1939, the Income-tax authorities served a notice on the assessee under Section 34 (1) and assessed them on August 20, 1940, on the profits earned by the firm from September 29, 1936, to October 8, 1937, on the basis of Section 26 (2) as it stood before it was amended by the Income-tax Amendment Act of 1939. The assessee contended (i) that they were not successors to the firm inasmuch as one item of gross profit was not taken over by them, and (ii) that since the assessment was made in 1940, Section 26 (2) as amended by the Income-tax Amendment Act of 1939, applied to them and therefore they were only liable to be assessed in respect of the period during which they carried on business.

Held, (i) that the assesses were successors to the firm within the meaning of Section 26 (2) of the Act ;

(ii) that the assessment was to be made as if it were one which was effected in the year in which escapement had been effected, namely 1938-39, and as at that time the provisions of the Amendment Act were not in force, the Income-tax Authorities were right in making an assessment on the basis of Section 26 (2) as it stood before it was amended by the Act of 1939.

Reference by the Income-tax Appellate Tribunal, Calcutta Bench, under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by the Income-tax (Amendment) Act of 1939 : (No. 5 of 1941).

STATEMENT OF CASE.

"This is the first application of its kind before this Bench of the Income-tax Appellate Tribunal under Section 66 (1) for a reference to the High Court and arises out of the order, dated the 28th March, 1941, passed by this Tribunal. It may be stated at the outset that the provisions of Section 66 (1) as they stand after the Amendment Act of 1939 are slightly different and the case to be stated may therefore be a little different in presentation from what it has been hithertofore. The Income-tax Act as it stood before the amendment required the Commissioner to submit his statement of the case to the High Court "with his own opinion thereon" while the Income-tax Appellate Tribunal which is a new body constituted by the Income-tax Amendment Act, 1939, has not been required to give its opinion on the question to be so referred. This difference is obviously due to the fact that the Commissioner had to state a case as arising out of the order of the Appellate Assistant Commissioner and had therefore to give his own view of the matter for consideration, while the Tribunal has to state a case as arising out of its own appellate order wherein its "own opinion" is already fully recorded.

2. Before proceeding to examine the questions stated by the applicant, we may give briefly the facts leading up to this application.

3. The Income-tax Officer, Companies District III, Calcutta, initiated proceedings against the applicant by issuing a notice under Section 34 for 1938-39 in June, 1939, and the resultant assessment was completed by him on the 20th August, 1940—*vide* his order of that date. He found that the appellant had "succeeded" to the business of Messrs. Jaidayal Sagarmall of Benares and on this finding made an assessment under Section 26 (2) of the Income-tax Act as it stood in 1938-39.

In the appeal before the Appellate Assistant Commissioner it was contended that the finding of the Income-tax Officer on the question of 'succession' was wrong but it was rejected.

4. The applicant Company then came before the Income-tax Appellate Tribunal by virtue of the amended provision of Section 33 (1) and the Tribunal went into the matter and recorded its own findings confirming the orders below. The order on appeal was passed by the Tribunal on the 28th March 1941 and the reasons for the view taken by this Tribunal are fully stated in its order. In the main the reasons for the finding were that no part of the business was left over and that the evidence on record led to the conclusion that it was a case of succession.

5. The applicant in his application forwarded with letter dated the 26th May 1941 wanted the following questions to be referred to the High Court :—

(a) That where an assessee purchased from the vendors certain assets excluding the business debts, outstandings and its other activities which were retained by the vendors and continued as before, could the assessee be treated as successors to the vendors under Section 26 (2) of the old Act and assessed as such.

(b) That where a notice under Section 34 of the Income-tax Act was issued in or about June 1939 under the new Act as amended, which came into force before the said notice was issued in respect of the assessment for the year 1938-39, whether the said assessment was to be governed by the old Act or the new Act under which the notice was issued.

The applicant has assumed several facts which are not found in the order of the Tribunal. The reference has to arise out of the order passed by the Tribunal and not on assumed facts set up by the applicant. Question in para. (a) will not arise as the Tribunal has found as a fact that the facts mentioned in the aforesaid question are not proved.

6. The applicant by a further application dated the 7th July sought to modify the question to be referred to the Hon'ble High Court in the following words :—

“(i) Whether in the facts and circumstances of this case Section 26 (2) becomes applicable, and

(ii) assuming that Section 26 (2) became applicable whether the proceeding for assessment, which was commenced and concluded under the new Act, should impose liability of tax to the successor when the predecessor was available for assessment simply because the year of assessment happened to be the year 1938-39.”

7. We do not however propose to refer the question No. (1) in the amended form stated by the applicant as above for that would lead to the examination of the facts by the High Court which their Lordships of the Privy Council have not approved. In *Commissioner of*

*Income-tax v. Laxminarain Badridas*¹, their Lordships have been pleased to observe :

"Nor is it possible to turn a mere question of fact into a question of law by asking whether as a matter of law the officer came to a correct conclusion upon a matter of fact."

What could be a question of law would be whether on the facts as found by the Appellate Tribunal, a case of succession has been made out as formulated.

8. The Appellate Tribunal had to consider whether the applicant has succeeded to the business of the vendor and in coming to this finding had to take several facts into consideration and mainly the following facts :—

(1) The applicant Messrs. Krishna Hydraulic Press Ltd., is a private company promoted by the vendors, Jaidayal Sagarmal who hold substantial part of the share capital of Rs. 2,00,000. The Company was formed on the 3rd March 1938 for the main purpose of taking over and purchasing as a going concern the business of Jute, Hemp Press, Oil Mills and Iron foundry, carried on at Seopur in Benares by Messrs. Jaidayal Sagarmal (Sagarmal Prabaladka and others), under the name and style of "Krishna Mills" together with all land, buildings, machineries and other appurtenances attaching thereto. An agreement had been entered into between the vendor and the appellant for such taking over and in pursuance of such agreement, movable properties consisting of loose plants, machineries, tools, implements and other movable properties of the value of Rs. 2,00,000 were delivered to the appellant before the 4th March 1938, and on the 4th March 1938, sale deed for a sum of Rs. 1,00,000 was executed by the vendor in favour of the applicant in respect of immovable properties consisting of land, buildings, fixed machineries and other immovable properties of the said Mill and Press and other legal incidents thereof, together with the goodwill of the said business, and the right to use the name of Krishna Mills and Press and benefit of all contracts and all legal incidents of the said Krishna Mills and Press.

(2) In June 1939, notice under Section 34 was issued to the applicant for the assessment for the year 1938-39 in respect of the business of the predecessor taken over by the applicant and on the 30th June 1939 the applicant wrote to the Income-tax Officer that the company's business was taken over as a running concern.

(3) The statement that the stores and the book debts were not taken over was not proved and was against the recital in the sale deed,

(1) (1937) 5 I.T.R. 170, at p. 179.

dated the 4th March 1938. As a matter of fact the applicant failed to satisfy by evidence that any part of the business was left over.

9. The applicant in his application stated several incorrect facts and attributed to the Bench several findings of fact in paragraph 8 of his application, but our findings of fact have already been stated in the last part of our order. The only challenge to the finding of the Appellate Assistant Commissioner on the question of succession before the Tribunal was that it was a case of partial succession. We held that it was not proved that the case was of partial succession and as a matter of fact the omission to examine the vendors led us to think that the statement regarding partial succession was not proved. We did not accept the statement of the applicant that book debts and stores were not purchased and we have definitely held that this allegation has not been proved. In this view of the matter there was a succession of the entire business.

10. The Departmental Representative referred us to *Thomson and Balfour v. Le Page*¹, *Wilson and Barlow v. Chibbett*² and *Malayalam Plantations, Ltd. v. Clark*³ to show that the question of succession is a question of fact. He submitted that in view of the findings of the Tribunal no question of law could, in any case, arise in this particular case as no legal difficulty as to the application of the phrase "succeeded in the same capacity" was involved here. The view we take of the matter is that whether the facts found amount in law to succession is a question of law but the facts found are not to be disturbed. There are the following Indian cases, *G. I. M. Gregory & Co., In re*⁴, and *Commissioner of Income-tax, Burma v. S. Mansookhlal Zaveri*⁵ on the question of succession.

11. Whether under the law these facts would amount to succession or not would be a question of law. We therefore modify the question No. (i) in the following form :—

"Whether on the facts found by the Appellate Tribunal a case of 'succession' as contemplated by Section 26 (2) has been made out."

12. The second question which has been formulated by the applicant in the amended application quoted above may be modified as under :—

"Whether the assessment for the year 1938-39 made in 1939-40 was correctly made on the basis of Section 26 (2) as it stood before it was amended by the Income-tax Act of 1939?"

This latter is essentially a question of law and we have no hesitation in making a reference.

(1) (1923) 8 Tax Cas. 541, at p. 549.

(2) (1929) 14 Tax Cas. 407, at p. 412.

(3) (1935) 19 Tax Cas. 314, at p. 323.

(4) (1937) 5 I.T.R. 12, at p. 42.

(5) (1937) 5 I.T.R. 664, at p. 673.

13. The record will be submitted to the High Court with necessary annexures including assessment order, order of the Appellate Assistant Commissioner, order of the Appellate Tribunal, the first application made by the appellant, reply by the Departmental Representative and the second application made by the applicant.

14. We had asked the parties as required by the Rules of the Tribunal to come to an agreed statement of facts but the applicant has not been able to agree on the facts. We have to make our statement of the case as stated above in the absence of agreed statement and submit the above statement of the case for such decision as the High Court may be pleased to give in the case."

[On the second point the opinion of the Appellate Tribunal as stated in the Judgment of the Tribunal delivered under Section 33 of the Act was as follows:—]

"In regard to the second point the appellant did not quote any authority for his proposition. The case *Jattu Shah Nathu Shah v. Commissioner of Income-tax, Punjab*¹, referred before the Appellate Assistant Commissioner was repeated. It has been held that it is the making of the assessment and the date thereof that determines the applicability of the law governing such assessment. The case of *Commissioner of Income-tax, Bombay v. Sind Hindu Provident Fund Society*² has been cited by the respondent. It has been held in the said ruling that the law and statutory rules applicable for determining assessment are the law and statutory rules in force for the year of assessment. In the year of assessment 1938-39 under Section 26 (2) of the Income-tax Act, the successor was liable for the predecessor's income of the "previous year." By the Amending Act 1939, this was changed and from 1st April 1939, each was made responsible for his profits. The Amending Act did not enact that this provision will have retrospective effect. It is a fundamental rule of law that no statute shall be construed to have a retrospective operation unless such a construction appears clearly in the terms of the Act or arises by necessary implication. (*Maxwell on The Interpretation of Statutes*, quoted in *Ingle v. Farrand*³). The said rule will apply to the Indian conditions and the amendment to Section 26 (2) in 1939 has not been enacted to have such retrospective effect to deprive the Crown of the right it had in the year of assessment. Following the said two decisions, we find the assessment for 1938-39 was rightly made on the basis of the Act in force in that year. No other point is pressed and the appeal is, therefore, dismissed."

(1) (1932) 6 I.T.C. 162.

(2) (1940) 8 I.T.R. 467.

(3) (1927) 11 Tax Cas. 446, at p. 468.

dated the 4th March 1938. As a matter of fact the applicant failed to satisfy by evidence that any part of the business was left over.

9. The applicant in his application stated several incorrect facts and attributed to the Bench several findings of fact in paragraph 8 of his application, but our findings of fact have already been stated in the last part of our order. The only challenge to the finding of the Appellate Assistant Commissioner on the question of succession before the Tribunal was that it was a case of partial succession. We held that it was not proved that the case was of partial succession and as a matter of fact the omission to examine the vendors led us to think that the statement regarding partial succession was not proved. We did not accept the statement of the applicant that book debts and stores were not purchased and we have definitely held that this allegation has not been proved. In this view of the matter there was a succession of the entire business.

10. The Departmental Representative referred us to *Thomson and Balfour v. Le Page*¹, *Wilson and Barlow v. Chibbett*² and *Malayalam Plantations, Ltd. v. Clark*³ to show that the question of succession is a question of fact. He submitted that in view of the findings of the Tribunal no question of law could, in any case, arise in this particular case as no legal difficulty as to the application of the phrase "succeeded in the same capacity" was involved here. The view we take of the matter is that whether the facts found amount in law to succession is a question of law but the facts found are not to be disturbed. There are the following Indian cases, *G. I. M. Gregory & Co., In re*⁴, and *Commissioner of Income-tax, Burma v. S. Mansookhlal Zaveri*⁵ on the question of succession.

11. Whether under the law these facts would amount to succession or not would be a question of law. We therefore modify the question No. (i) in the following form :—

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12. The second question which has been formulated by the applicant in the amended application quoted above may be modified as under :—

"Whether the assessment for the year 1938-39 made in 1939-40 was correctly made on the basis of Section 26 (2) as it stood before it was amended by the Income-tax Act of 1939 ?"

This latter is essentially a question of law and we have no hesitation in making a reference.

(1) (1923) 8 Tax Cas. 541, at p. 549.

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(5) (1937) 5 I.T.R. 664, at p. 673.

13. The record will be submitted to the High Court with necessary annexures including assessment order, order of the Appellate Assistant Commissioner, order of the Appellate Tribunal, the first application made by the appellant, reply by the Departmental Representative and the second application made by the applicant.

14. We had asked the parties as required by the Rules of the Tribunal to come to an agreed statement of facts but the applicant has not been able to agree on the facts. We have to make our statement of the case as stated above in the absence of agreed statement and submit the above statement of the case for such decision as the High Court may be pleased to give in the case."

[On the second point the opinion of the Appellate Tribunal as stated in the Judgment of the Tribunal delivered under Section 33 of the Act was as follows:—]

"In regard to the second point the appellant did not quote any authority for his proposition. The case *Jattu Shah Nathu Shah v. Commissioner of Income-tax, Punjab*¹, referred before the Appellate Assistant Commissioner was repeated. It has been held that it is the making of the assessment and the date thereof that determines the applicability of the law governing such assessment. The case of *Commissioner of Income-tax, Bombay v. Sind Hindu Provident Fund Society*² has been cited by the respondent. It has been held in the said ruling that the law and statutory rules applicable for determining assessment are the law and statutory rules in force for the year of assessment. In the year of assessment 1938-39 under Section 26 (2) of the Income-tax Act, the successor was liable for the predecessor's income of the "previous year." By the Amending Act 1939, this was changed and from 1st April 1939, each was made responsible for his profits. The Amending Act did not enact that this provision will have retrospective effect. It is a fundamental rule of law that no statute shall be construed to have a retrospective operation unless such a construction appears clearly in the terms of the Act or arises by necessary implication. (*Maxwell on The Interpretation of Statutes*, quoted in *Ingle v. Farrand*³). The said rule will apply to the Indian conditions and the amendment to Section 26 (2) in 1939 has not been enacted to have such retrospective effect to deprive the Crown of the right it had in the year of assessment. Following the said two decisions, we find the assessment for 1938-39 was rightly made on the basis of the Act in force in that year. No other point is pressed and the appeal is, therefore, dismissed."

(1) (1932) 6 I.T.C. 162,

(2) (1940) 8 I.T.R. 467.

(3) (1927) 11 Tax Cas. 446, at p. 468.

JUDGMENT.

GENTLE, J.—Prior to the month of March 1938, a firm named Jaidayal Sagarmal carried on a business of jute, hemp press, oil mills and iron foundry in Benares. The applicants, Krishna Hydraulic Press Ltd., were incorporated on March 3, 1938, the main purpose of the company being to take over and purchase as a going concern the business of Jaidayal Sagarmal together with all land, buildings, machinery, and other appurtenances attached thereto. After the company's incorporation a sale deed was executed on March 4, 1938, by which, in consideration of a sum of one lac of rupees, the company obtained immovable properties consisting of land, buildings, fixed machinery and other immovable properties of the mill and press and other legal incidents together with the good-will of the business and the right to use the name of Krishna Mill and Press and benefit of all contracts and all legal incidents of the Krishna Mills. The company has carried on that business ever since it was acquired on March 4, 1938.

On June 10, 1939, a notice was served upon the company under Section 84 (1) of the Income-tax Act in respect of an assessment which should have been made in the year 1938-39. On August 20, 1940, the assessment was completed and the company was assessed in a sum of Rs. 14,723. The assessment was made upon the profits of the concern from September 29, 1936, to October 8, 1937. It has been held by the Appellate Tribunal that the company is the successor to the firm of Jaidayal Sagarmal and alone is liable to be and had been assessed in respect of the profits during the year, the subject of assessment.

Two questions which now come for consideration are: (i) Whether on the facts found by the Appellate Tribunal a case of succession as contemplated by Section 26 (2) has been made out?

(2) Whether the assessment for the year 1938-39 made in 1939-40 was correctly made on the basis of Section 26 (2) as it stood before it was amended by the Income-tax Act of 1939?

So far as succession is concerned the only point in the argument on behalf of the company that it did not succeed and is not the successor of the business of the old firm is by reference to one entry in a profit and loss account which was supplied by the company and is attached to the application under Section 66 (1) of the Act. In this profit and loss account the total receipts of the firm amount to Rs. 41,446-9-3, the expenses amount to Rs. 8,860-15-9 and the difference between the expenses and the receipts is the sum of Rs. 32,580-14-9. Among the receipts under the heading "Hemp a/c," is a sum of Rs. 5,353-8-3. In the assessment a deduction has been made, under the head of "Profit from dealing with hemp (not taken

over by this company)," of Rs. 5,854/-. From this it is argued that the company did not succeed to the firm as it did not take over its hemp business. What the reasons were for this sum being deducted does not appear.

By the sale deed of March 4, 1938, which was executed by the company and in respect of which according to the deed, one lac of rupees was paid, the company acquired all the immovable properties including land, buildings, machinery, and so on, together with the goodwill of the business and the right to use the name of Krishna Mills and Press and the benefit of all contracts and legal incidents. Whilst one item of gross profit was omitted, in my view that is not sufficient to show that the company are not the successors to the firm. But the matter does not rest there. Fifteen months after the company was incorporated and obtained by means of a sale deed the assignment of the assets of the firm, its managing agents wrote on June 30, 1939, as follows:—

"The present business of Krishna Hydraulic Press Ltd. was taken over from Messrs. Jaidayal Sagarmal of Nandsah Mohalla, Benares, on the 3rd March 1938 as a running concern and this company is working the press on and from the same date, *i.e.*, 3rd March 1938."

It has been conclusively shown that the company are the successors to the firm and that the business which the company conducts is that which was previously carried on by the firm prior to the incorporation of the company.

The next question which arises is in regard to the provisions of Section 26 (2) of the Income-tax Act. By the Amending Act of 1939 a substitution was made in this section. The 1939 Act came into force on March 31 of that year. Section 26 (2) originally provided that when one person succeeded to the business of another person, the person succeeding was liable for the whole of the income-tax ascertained from the profits of the year previously whilst the person succeeded was carrying it on. The substituted section provides that the succeeding person and the person succeeded shall respectively be assessed for their actual shares, if any, of the income, profits and gains of the previous year.

On behalf of the applicant company it was argued that since the assessment was made in the year 1940-41, although it is in respect of the year 1938-39, and since the substituted Section 26 (2) was in force at the time the assessment was made, its provisions should apply. Consequently the applicant company should only be assessed in respect of the period during which it carried on the business and should not be assessed in respect of the whole of the profits for the year prior to the year 1938-39.

It is conceded that the assessment has been made under Section 34 (1) of the Income-tax Act, which is known as the escaping section. So far as is material, the section provides as follows:

"If in consequence of definite information which has come into his possession the Income-tax Officer discovers that income, profits or gains chargeable to income-tax have escaped assessment in any year . . . the Income-tax Officer may, in any case in which he has reason to believe that the assessee has concealed the particulars of his income . . . serve in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of Section 22, and may proceed to assess or re-assess such income, profits or gains, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section."

The words which require particular attention are "have escaped assessment in any year." The assessment which was made in August 1940 was in respect of the year 1938-39 and it was made because in the year of assessment the company escaped assessment in that year and the provisions of the section can only be called into effect when, as is material, the Income-tax Officer has reason to believe the assessee has concealed the particulars of his income. This section enables an assessment to be made in a subsequent year when the assessee has escaped from being assessed. From what has he escaped? He has escaped from an assessment which would have been made upon him during an earlier year. The object of the section is to overcome the result of an assessee escaping from an assessment which should have been made upon him. Another object, of course, is that there may be recovery from him of income-tax which he should have paid had the assessment been made during the correct period. From this, in my view, it must follow that the assessment made in a subsequent year must be the same as the assessment would have been, had it been made in the correct year. The fact that legislation has changed meanwhile does not in my view alter the circumstances. The assessment from which the company escaped in 1938-39 was an assessment in respect of the whole of the profits of the business to which it succeeded and which were made during the year of account, namely, the income-tax year immediately prior to the year 1938-39.

Attention has been drawn by the learned Advocate on behalf of the company to the concluding words of Section 34 (1) that the "Income-tax Officer may proceed to assess" and "the provisions of this Act shall, so far as may be, apply as if the notice were a notice issued under Section 22 (2)."

It was argued that at the time when the assessment

in fact was made the provisions of the Act which were in force at that period should be applicable. In my view the assessment is to be made as if it were one which was effected in the year in which escapement has been obtained, in this case in the year 1938-39, and the provisions of the Act do not apply since they would not have applied at the time the assessment should have been made.

For these reasons, in my view, the answers to the two questions should both be in the affirmative. There will be no order as to costs.

DERBYSHIRE, C. J.—I agree.

Reference answered in the affirmative.

[IN THE PRIVY COUNCIL.]

RAJA BAHADUR KAMAKSHYA NARAIN SINGH OF RAMGARH
v.

COMMISSIONER OF INCOME-TAX, BIHAR AND ORISSA.

LORD RUSSELL OF KILLOWEN, LORD WRIGHT, LORD PORTER,
SIR GEORGE RANKIN AND SIR MADHAVAN NAIR.

May 13, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 3, 6, 12—MINING LEASE—ROYALTY BASED ON ACTUAL TONNAGE OF COAL, SALAMI AND MINIMUM ROYALTY—WHETHER INCOME OR CAPITAL—MEANING OF INCOME—NATURE OF MINING LEASES.

The assessee received large payments by way of royalty under various mining leases. The leases purported to grant and demise unto the lessees for 999 years the underground coal mining rights specified in the schedule to the leases and all the estate, right, title and interest of the lessor into and upon the same and every part thereof with full liberty and power to the lessees to search for, work, make merchantable and carry away the coal there found and with power to dig and sink pits, to erect engines, machinery, buildings, workshops, cottages and to make such railways, tramways, and roads as are required. In return for these rights the lessees were to pay a sum by way of salami or premium and an annual sum as royalty computed at a certain rate per ton on the amount of coal raised and coke manufactured, subject always to a minimum annual sum. The lessor had the right to re-enter in case of failure to pay the rent or royalties. It was contended on behalf of the assessee that the sums received as salami and royalty did not constitute income but were capital receipts representing the price of the minerals removed.

Held, affirming the decision of the High Court at Patna, (i) that the salami was paid for the acquisition of the right of the lessees to enjoy the benefits granted to them by the lease and that right being a capital asset, the money paid to purchase it was a payment on capital account;

(ii) that the minimum royalty being a species of annual guarantee was income flowing from the covenants in the lease and was in no sense a payment on capital account;

(iii) that it was fallacious to envisage the royalty payable every year under the terms of the lease as merely the price of the actual tons of coal; it was compensation which the lessees paid the lessor for that species of occupation which the contract between them allowed and it was therefore income from other sources within the meaning of Section 12 of the Act.

If the receipts are income, it is not material for tax purposes that that for which they are paid comes from a wasting property.

Definition of income in *Commissioner of Income-tax, Bengal v. Shaw Wallace and Co.* [1932] (59 Cal. 1343; 59 I.A. 206) considered.

Commissioner of Income-tax, Bihar and Orissa v. Kumar Kamakshya Narain Singh [1940] (8 I.T.R. 563) affirmed.

Cases referred to :

Alianza Co., Ltd. v. Bell (1905) 1 K.B. 184 affirmed in 1906 A.C. 18; 75 L.J.K.B. 44; 93 L.T. 705; 54 W.R. 413; 22 T.L.R. 94; 50 S.J. 74; 5 Tax Cas. 172.

Coltess Iron Co. v. Black (1881) 6 A.C. 315; 29 W. R. 717; 46 J. P. 20; 1 Tax Cas. 287.

Commissioner of Income-tax, Bengal v. Shaw Wallace & Co. (1932) A.I.R. 1932 P.C. 138; 136 I.C. 742; 59 Cal. 1343; 59 I.A. 206.

Gowan v. Christie 1873 (2 Scotch App. 273).

Gopal Saran Narayan Singh v. Commissioner of Income-tax, Bihar & Orissa (1935) A.I.R. 1935 P.C. 143; 156 I.C. 856; 14 Pat. 552; 62 I.A. 207; 3 I.T.R. 237.

Manindra Chandra Nandi v. Secretary of State (1907) 34 Cal. 257; 5 C.L.J. 148.

R. v. Westbrook (1875) 10 Q.B. 178; 2 New Sess. Cas. 599; 16 L. J. M. C. 87; 11 Jur. 515.

Scoble v. Secretary of State (1903) 1903 A.C. 299; 72 L.J.K.B. 617; 89 L.T. 1; 51 W.R. 675; 4 Tax Cas. 618; 19 T.L.R. 550.

Shiv Prasad Singh v. Emperor (1924) A.I.R. 1924 Pat. 679; 82 I.C. 653; 4 Pat. 73.

Privy Council Appeal No. 21 of 1942. Appeal from a judgment of the Patna High Court reported in [1940] (8 I.T.R. 563).

Sir Walter Monckton, Cyril King and R. K. Handoo, for the Appellant.

J. Millard Tucker and Sir Alfred Wort, for the Respondent.

JUDGMENT.

LORD WRIGHT.—This is an appeal from a judgment of the High Court at Patna, dated 6th September 1940, in a reference under Section 66 of the Income-tax Act (Act XI of 1922) (as amended by Acts XXI and XXII of 1930 and Act XVIII of 1933), by which the High Court answered

a question of law submitted by the Commissioner of Income-tax of Bihar and Orissa, in the negative, in respect of an assessment to income-tax of the appellant assessee for the year 1937-38. Two questions had been submitted to the Commissioner by the assessee to be referred to the High Court which were :

(1) Whether royalty on mines being capital revenue should not have been excluded in computing the total income determined for income-tax ? (2) What should be the principle on which cost of management in collection of royalties is to be determined when there is a combined management covering both the zamindari collection of agricultural income and royalties of mines ?

The Commissioner of Income-tax was of the opinion that the second question raised no question of law and should not be answered by the High Court. In fact, no argument was addressed by the assessee to the High Court thereon, and the High Court concurred in the opinion of the Commissioner of Income-tax. No further reference to that question need therefore be made. The assessee, Kumar Kamakshya Narain Singh Bahadur, is and was at all material times the proprietor of a revenue paying estate known as the Ramgarh Raj, bearing tauzi No. 28, in the Collectorate of Hazaribagh, being impartible and governed by the rule of primogeniture. At the time of the assessment which is the subject-matter of this appeal, the estate was under the management of the Court of Wards, the assessee being a minor. On 10th August 1937, the assessee attained his majority and the estate was released from the management of the Court of Wards. For the income-tax year 1937-38 the manager of the estate on behalf of the assessee made a return of the income of the assessee to the Income-tax Officer, District Hazaribagh, including a sum of Rs. 5,32,368-2-10 being royalties realised from lessees of coal mines under seven leases, each of them for a term of nine hundred and ninety nine years, in the form of and on similar conditions and covenants as those contained in three leases, that is to say : (1) A lease dated 5th April 1919, between Alexander McNeil Walter the Manager of the Ramgarh Estate under the Court of Wards Act (Act IX Bengal Code 1879) of the one part and Bokaro and Ramgur Limited of the other part ; (2) a lease dated 25th March 1925, between the said Alexander McNeil Walter and Bokaro and Ramgur Limited of the other part ; (3) a lease dated 12th April 1927, between the said Alexander McNeil Walter of the one part and the Karanpura Development Company Limited of the other part. Under the terms of the leases the lessees covenanted to pay to the lessors royalties on all steam coal, rubble coal, dust, hard and soft coke, gotten, manufactured and despatched, the lessee also covenanting that

after certain dates as provided by the said leases minimum royalty should be paid on the terms and at the rates provided therein, in the event of the royalties reserved and payable under the said leases not amounting to the figure of the minimum royalty.

The Income-tax Officer of Hazaribagh assessed the assessee to income-tax on the income of the assessee including the coal mine royalties in the sum of Rs. 76,286-9-0 and to super tax in a sum of Rs. 1,95,610-4-0. By a petition of appeal dated 15th September 1937, the assessee appealed to the Assistant Commissioner of Income-tax on the following amongst other grounds: "That according to law, rent and royalty on mines being capital revenue, that is value of the corpus, should be exempted in assessing income-tax; that rent and royalty are in the nature of the price of coal and instalments of purchase money and hence not assessable to income-tax. By his order of 14th February 1938, the Assistant Commissioner expressed the opinion that royalties should be included in assessing the income of the assessee and stated that:

"in order to constitute a sale a fixed price is always essential. But while the lessees are to pay royalties at a certain fixed rate per ton of coal extracted, the aggregate of such payments must not be less than a minimum sum in any year. This minimum has to be paid even if no coal is extracted. From this it follows that royalty is not the price of coal taken as the assessee contends."

The assessment was confirmed. By a petition under Section 33 of the Act to the Commissioner of Income-tax the assessee prayed that the Commissioner should send for the record and that the order of the Assistant Commissioner be set aside and a fresh assessment be made, which petition was rejected. By an application under Section 66 (2) of the Act the assessee required the Commissioner of Income-tax to refer the two questions set out above for decision of the High Court. On 23rd December 1938, the Commissioner of Income-tax drew up a statement of the case exhibiting a specimen of the mining leases concerned referring these questions to the High Court, and expressed his own opinion upon them, which was, as regards the first question: (a) Receipts under leases in the terms of the exhibit were rightly held by the appellate officer to be annual income and not capital instalments of a purchase price. The High Court referred the case to a Full Bench (the Honourable Sir Trevor Harries, C.J., the Honourable Fazl Ali, J., and the Honourable Manohar Lall, J.,) who were of the opinion that royalties received by the assessee were "income from other sources" within the meaning of Sections 6 (vi) and 12 (1) of the Act, and were rightly assessed to income-tax by the taxing authorities. It is here only

necessary to refer in detail to the material terms and covenants of one of the leases, namely, that dated 3rd April 1919. The most material clause was as follows :

“This indenture witnesseth that in pursuance of the said agreement and in consideration of the salami or premium rupees thirty-seven thousand and forty (being at the rate of rupees forty per standard bigha on nine hundred and twenty-six bighas) in respect of the premises at or before the execution of these presents by the lessees paid to the lessor (the receipt whereof the lessor doth hereby admit and acknowledge) the lessor doth hereby grant and demise unto the lessees all and singular the under-ground coal mining rights of and in all those the lands and premises specified in schedule hereto and which are hereinafter referred to as the premises and all the estate right title interest claim and demand of the lessor into and upon the same and every part thereof with full liberty and power to the lessees to search for work make merchantable and carry away the coal there found and also liberty and power for the purposes aforesaid and all other purposes connected therewith to dig sink drive make repair and use all such pits shafts drifts levels water gates planes adits water-ways and air-ways and to form and erect engines machinery dressing floors buildings workshops store houses cottages godowns coke ovens furnaces brick-kilns lime-kilns erections and things and to form all such railways and tramways and other roads and communications spoil heaps and other conveniences in over and under the said lands as may be necessary in the premises. To hold the said premises hereby demised unto the lessees from the first day of November one thousand nine hundred and fifteen for the term of nine hundred and ninety-nine years subject to the right of determination hereinafter contained yielding and paying therefor unto the lessor by monthly payments in each year the first such payments to be made on the twenty-first day of December one thousand nine hundred and fifteen the royalty on all coal and coke raised gotten manufactured and despatched from the said lands hereby demised at the rates following that is to say :—Four annas per ton on all steam coal, three annas per ton on all rubble coal and two annas per ton on all dust coal raised and despatched and eight annas per ton on all hard coke and six annas per ton on all soft coke manufactured and despatched.”

The lease provided for payment of a minimum royalty at the end of any year in which royalties on coal raised and despatched should be less than a certain amount. It also contained usual covenants and in particular that the lessees undertook to deliver up the mines in good order and condition at the end or sooner determination of the term. It included a covenant by the lessor for quiet enjoyment and the lessees

were granted liberty to determine the lease on certain terms. The lessors were further entitled to enter upon the demised premises and to determine the lease on specified conditions if the royalties were not duly paid. The other leases were in terms similar for all purposes material to this appeal to the lease just referred to. The appellant's main contention has been that on the true construction of the Income-tax Act, 1922, mineral royalties depending on the tonnage of minerals raised and despatched are not properly chargeable to tax because they are in their nature and quality capital, and are not "income" or income derived from "other sources" within the meaning of Sections 6 and 12 of the Act.

The Indian Income-tax Act of 1922, which was a consolidating Act, is both in its general framework and its particular provisions different from the English Income Tax Acts, so that decisions upon the English Acts are in general of no assistance in construing the Indian Act. But on some fundamental concepts reference may be to some extent usefully made to English decisions, in particular as to the meaning of the word "income." Under Section 4 of the Indian Act it is provided that the Act shall apply to all "income, profits or gains" described or comprised in Section 6, and arising in British India. Section 3 specifies six heads of income, profits and gains which are to be chargeable. Of these it is not disputed that the monies upon which the disputed charge has been assessed (if taxable as income under Section 6), fall under the head "other sources." As to this head, Section 12 enacts (1) that the tax payable by an assessee under that head is to be

"in respect of income, profits and gains of every kind and from every source to which the Act applies (if not included under any of the preceding heads)."

(2) Sub-section (2) provides that :

"Such income, profits and gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains, provided that no allowance shall be made on account of any personal expenses of the assessee."

Under the English Acts income which consists of mining royalties, was taxed under Schedule A but according to the relevant rules of Schedule D. Under the Indian Act the provisions of Section 9 with reference to "property" (which is head III in Section 6) are regarded as excluding royalties from being held to come under that head. Royalties cannot be regarded as "profits or gains" of a business. The sources of the royalties may properly be deemed to be the lessees' covenants to pay them, and hence royalties fall under "other sources."

The appellant's substantial argument is that the coal on his land is capital, and that the sums which he receives from time to time for each ton raised and despatched is a capital receipt, being the price given in exchange for the capital asset, as and when the property in each ton vests in the lessee. He supports this contention also on what he terms are the realities and equities of the position. These, as he urges, arise from the circumstance that the coal is a wasting property and is being gradually exhausted as each ton is raised and disposed of. He has also submitted, though not perhaps very strenuously, that whereas under the English Acts mines and income from them are expressly dealt with and are clearly therefore subjected to the tax, the position under the Indian Act is different in the respect that mining royalties are not expressly specified as taxable. He has also contended that their peculiar characteristics make the general words "income, profits and gains" inapplicable to them, at least in the absence of their being expressly mentioned.

The issue depends on the true interpretation of the word "income" as used in the Act. Income is not only the most general word in Section 6 of the Act, but is obviously a more appropriate term to be applied to mining royalties than "profits or gains." In order to ascertain whether the word "income" applies to mining royalties, it is necessary to advert to the nature of a mining lease and the meaning of rent or royalties as used in a mining lease. A question has been raised whether the mining leases are leases within Sections 105 to 108 of the Transfer of Property Act, 1882, or within the ordinary legal acceptance of that word in Indian law. In their Lordships' opinion, the leases are properly described as leases according to ordinary parlance and are within the terms of the sections referred to of the Act of 1882. At the same time, their Lordships do not regard this question as relevant to determine in the present case.

The payments which under the leases are exigible by the lessor may be classed under three categories: (i) the salami or premium; (ii) the minimum royalty; (iii) the royalties per ton. The salami has been, rightly in their Lordships' opinion, treated as a capital receipt. It is a single payment made for the acquisition of the right of the lessees to enjoy the benefits granted to them by the lease. That general right may properly be regarded as a capital asset, and the money paid to purchase it may properly be held to be a payment on capital account. But the royalties are on a different footing. The minimum royalty is only payable if in any year the royalties on coal raised and despatched are less than the sum fixed as the minimum royalty. This amounts to a species of annual guarantee: it does not correspond to any coal in fact

extracted and taken away: it is simply "income" flowing from the covenants in the lease, contingently on the lessees' failure to take the minimum quantity of coal. It would be payable if in any year the lessees took no coal at all, or if the coal in the mine was completely exhausted before the termination of the lease. The minimum royalty is therefore in their Lordships' judgment "income" and in no sense a payment on capital account. But the minimum royalty throws at least by analogy or contrast some light on the character of the royalties payable on each ton of coal. These in their Lordships' judgment, for reasons which will now be explained, constitute income, as the High Court at Patna has held in upholding the assessment. The appellant's case was primarily based on certain observations made by Lord Cairns in *Gowan v. Christie*¹. Lord Cairns said:

"for although we speak of a mineral lease, or a lease of mines, the contract is not, in reality, a lease at all in the sense in which we speak of an agricultural lease. There is no fruit; that is to say, there is no increase, there is no sowing or reaping in the ordinary sense of the term, and there are no periodical harvests. What we call a mineral lease is really, when properly considered, a sale out and out of a portion of land. It is liberty given to a particular individual for a specific length of time, to go into and under the land and to get certain things there if he can find them, and to take them away, just as if he had bought so much of the soil."

Lord Cairns was there not considering the question whether royalties under such a lease were capital or income for purposes of taxation. The question was whether the lessee was entitled to be relieved from his contract because he could not work the minerals at a profit. The House of Lords held against the lessee. Before discussing that dictum of Lord Cairns, certain other authorities may be cited. In *Coltness Iron Co. v. Black*², there was a further discussion of the nature of a mining lease. The main question was whether the lessees could deduct from their gross annual receipts, which included profits from their coal mines, the cost incurred in sinking new pits. The House held that they could not, because these costs were not part of the working expenses but were capital expenditure. They further rejected the contention that some allowance should be made against the profits because the coal was being gradually exhausted in the course of earning these profits. This, so far as it goes, is a decision against the appellant's argument. It is based on the English Taxing Acts under which mines are specifically assessed. Lord Blackburn, after quoting what Lord Cairns had said in *Gowan v. Christie*¹ went on to say:

(1) (1873) 2 Scotch App. 273, at p. 283.

(2) (1881) 6 A. C. 315; 1 Tax Cas. 287.

"But the argument that no income-tax should be imposed on what is, perhaps not quite accurately, called rent reserved on a mineral lease, because it is a payment by instalments of the price of minerals forming part of the land (any more than on the price paid down in one sum for the out and out purchase of the minerals forming part of the land), is, I think, untenable."

He further added in reference to the fact that the coal was being exhausted the following observations:

"It has also been sometimes argued that it is very unjust to tax at the same rate a terminable interest, such as that in a mine, which must at some time be worked out, and a fee simple interest, which will endure so long as this world continues in its present state. I will not inquire whether this is just or not. There is much force in the argument on the other side, that if the interest is terminable, so is the tax, and will cease when the interest ceases; but whether just or not, there can be no doubt that the same annual charge is imposed upon a terminable annuity and on one in perpetuity, and, what seems harder, that the same annual charge is imposed upon a professional income, earned by hard labour, often extending over many years before any return is got, and, when earned, precarious, as depending on the health of the earner."

Now it is true that Lord Blackburn was dealing with the English statutes which were clearly different from the Indian Act. Under the latter Act, the tax is on "income." Mines are not specially mentioned as they are in the English Act. But if income is in fact derived from mines, it is to be taxed as much as "income" from any other source. The general term covers the specific instances. The grounds on which the appellant contends that the royalties are not "income" are that they are capital receipts from a wasting property. In principle, in their Lordships' opinion, both these points are disposed of by Lord Blackburn's words, which depend on general principles, not on rules peculiar to the English Acts. Income, it is true, is a word difficult and perhaps impossible to define in any precise general formula. It is a word of the broadest connotation. Its definition has, however, been approached in recent decisions of this Board. The first to which their Lordships think it is desirable to refer is *Commissioner of Income-tax, Bengal v. Shaw Wallace & Co.*¹ Sir George Lowndes in delivering the judgment of the Board once more wisely emphasised the danger of using decisions on English Income Tax Acts in order to construe the Indian Act. He went on to give a definition of "income" as it is used in the Indian Income-tax Act. His definition was:

(1) (1932) 59 I.A. 206.

"Income, their Lordships think, in this Act connotes a periodical monetary return 'coming in' with some sort of regularity, or expected regularity, from definite sources. The source is not necessarily one which is expected to be continuously productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a mere windfall. Thus, income has been likened pictorially to the fruit of a tree, or the crop of a field. It is essentially the produce of something which is often loosely spoken of as 'capital.' But capital, though possibly the source in the case of income from securities, is in most cases hardly more than an element in the process of production."

That definition was followed and in substance repeated in a decision of the board delivered by Lord Russell of Killowen in *Gopal Saran Narayan Singh v. Commissioner of Income-tax, B. & O.*¹ In that case the appellant, the assessee, had transferred an estate in consideration of a lump sum and of the discharge of certain debts and of the payment to himself for life of an annuity of Rs. 2,40,000. It was held that the annuity constituted "income" to the assessee during each year in which it was paid. Lord Russell, adopting generally the definition already quoted, added the following important amplification:

"The word 'income' is not limited by the words 'profits' and 'gains.' Anything which can properly be described as income, is taxable under the Act unless expressly exempted."

It is not in their Lordships' opinion correct to regard as an essential element in any of these or like definitions a reference to the analogy of fruit, or increase or sowing or reaping or periodical harvests. Lord Cairns (*loc. cit*) used these expressions because he was distinguishing mineral leases from agricultural leases. Sir George Lowndes (*loc. cit*) speaks of "income" being likened pictorially to the fruit of a tree or the crop of a field. But it is clear that such picturesque similes cannot be used to limit the true character of income in general, and particularly when it is constituted by mining rent or royalties. These are periodical payments, to be made by the lessee under his covenants in consideration of the benefits which he is granted by the lessor. What these benefits may be is shown by the extract from the lease quoted above, which illustrates how inadequate and fallacious it is to envisage the royalties as merely the price of the actual tons of coal. The tonnage royalty is indeed only payable when the coal or coke is gotten and despatched: but that is merely the last stage. As preliminary and ancillary to that culminating act, liberties are granted to enter on the land and search, to dig and sink pits, to erect engines and machinery,

(1) (1935) 62 I.A. 207; 3 I.T.R. 237.

coke ovens, furnaces and form railways and roads. All these and the like liberties show how fallacious it is to treat the lease as merely one for the acquisition of a certain number of tons of coal, or the agreed item of royalty as merely the price of each ton of coal. The contract is in truth much more complex. The royalty is "in substance a rent; it is the compensation which the occupier pays the landlord for that species of occupation which the contract between them allows" to quote the words of Lord Denman in *R. v. Westbrook*¹. He was referring to leases of coal mines, clay pits and slate quarries. He added that in all these the occupation was only valuable by the removal of portions of the soil. It is true that he was dealing with occupation from the point of view of rating, but occupation has the same meaning in its application to matters of taxation such as are involved in this case.

There is, therefore, in their Lordships' judgment, no real justification for treating the royalties as capital payments. They think that they are "income" within the meaning of the Act, whatever may be the exact definition of that word in the Act. Its applicability may, in particular cases, differ because the circumstances, though similar in some respects, may be different in others. Thus the profit realised on a sale of shares may be capital if the seller is an ordinary investor changing his securities, but in some instances at any rate it may be income if the seller of the shares is an investment or an insurance company. Income is not necessarily the recurrent return from a definite source, though it is generally of that character. Income again may consist of a series of separate receipts, as it generally does in the case of professional earnings. The multiplicity of forms which "income" may assume is beyond enumeration. Generally, however, the mere fact that the income flows from some capital assets, of which the simplest illustration is the purchase of an annuity for a lump sum, does not prevent it from being income, though in some analogous cases the true view may be that the payments, though spread over a period, are not income, but instalments payable at specified future dates of a purchase price. Such a case is illustrated by *Scoble v. Secretary of State*². But, in their Lordships' judgment, the royalties here are clearly income and not capital. They are periodical payments for the continuous enjoyment of the various benefits under the leases. The actual acquisition of the property in a particular ton of coal at the moment when the lessees have cut and taken away the coal is only the final stage.

The authorities already cited and many others to the same effect show that the fact that the mines, which form an element in the

(1) (1875) 10 Q.B. 178.

(2) (1903) A.C. 299; 4 Tax Cas. 618.

consideration for the royalties, are wasting assets is irrelevant. The English cases are sufficiently collected and explained by the Court of Appeal in *Alianza Co., Ltd. v Bell*¹, affirmed in the House of Lords in 1906 A.C. 18². That case states principles which are generally applicable in India as well as in England. If the receipts are income, it is not material for tax purposes that that for which they are paid comes from a wasting property. If the payment ceases because the source ceases, so does the tax. Once it is established that the royalties are income within the meaning of the Act it is not material that the mines are in course of being exhausted unless there is provided in the Act that there should be a deduction from the income on that particular ground. But there is under the Indian Act no provision for allowance for amortisation in respect of the minerals being exhausted. Indeed, where as here the lease is for 999 years, an attempt to quantify the appropriate allowance would be scarcely practicable. However, Section 12 (2) already quoted in this judgment, expressly excludes allowances in respect of capital expenditure. Any ordinary expenditure incurred by the appellant in connexion with the leases, such as the cost of collection of the royalties, has been duly allowed. For these reasons which are substantially those given by the learned Judges of the High Court, their Lordships agree with them in their conclusions. Accordingly the appeal fails and should be dismissed.

Their Lordships in doing so are in agreement with the current of judicial opinion in the Indian Courts. They may start by citing the decision of the Calcutta High Court in *Manindra Chandra Nandi v. Secretary of State*³ and the elaborate judgment of Mookerjee, J., at page 283 which has never been dissented from in India. Similar views were expressed in the comparatively recent cases in the Patna High Court to which full reference has been made in the judgments under appeal. Their Lordships do not think it necessary to repeat here what has been so fully explained in these judgments. It is enough here to say that their Lordships substantially agree with them. They refer particularly to the judgment of Dawson Miller, C.J., in *Shiva Prasad Singh v. Emperor*⁴. It may be added that on the question at issue, there is no difference in principle between the effect of the Act of 1922 and its predecessor, the Act of 1886, in this matter. Their Lordships are of opinion that the judgment of the High Court should be affirmed and the appeal dismissed with costs. They will humbly so advise His Majesty.

Appeal dismissed.

(1) (1905) 1 K.B. 184,

(2) (1906) 5 Tax Cas. 172.

(3) (1907) 34 Cal. 257.

(4) (1924) 4 Pat 73

[IN THE ALLAHABAD HIGH COURT.]

LALA SARJU PRASAD, *In re*.

COLLISTER and BAJPAI, JJ.

September 1, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 13 PROVISIO, SEC. 31—ASSESSMENT UNDER SEC. 13 PROVISIO—APPEAL—POWER OF ASSISTANT COMMISSIONER TO SUBSTITUTE DIFFERENT METHOD OF COMPUTATION—CALLING FOR REPORT FROM INCOME-TAX OFFICER AND ALTERATION OF ASSESSMENT AFTER SUBMISSION OF REPORT—LEGALITY.

There is nothing in the Indian Income-tax Act to restrict, in respect to an assessment made under the proviso to Section 13, the powers which the higher authorities of the Department have under Sections 31 and 32 in respect to assessments generally. Consequently the Appellate Assistant Commissioner has jurisdiction, in an appeal against an assessment under the proviso to Section 13, to substitute a different method of computation for the method which has been adopted by the Income-tax Officer.

An Appellate Assistant Commissioner is entitled under Section 31 (2) to ask for a report from the Income-tax Officer in respect to an assessment and after submission of the report is entitled under Section 31 (3) either to confirm, or to reduce or to enhance the assessment.

Case referred to :—

Commissioner of Income-tax v. Pyare Lal Shukla (1942) 10 I. T. R. 239; 1942 A. L. J. 388.

Case stated under Section 66 (3) of the Income-tax Act by the Commissioner of Income-tax, C. P. and U. P.: (Miscellaneous Case No. 85 of 1938).

"In compliance with your Lordships' order, dated the 11th February, 1942, in Miscellaneous Case No. 85 of 1938, I have the honour to submit, for your Lordships' decision, under Section 66 (3) of the Indian Income-tax Act, 1922 (hereinafter referred to as "the Act"), the question of law set out in paragraph 3 below and held by your Lordships to arise out of the assessment for the year 1933-34 of Lala Sarju Prasad, son of Lala Faqirchand of Rasra, district Ballia, (hereinafter referred to as "the assessee"). The sections of the Act herein mentioned are as such sections stood before the Indian Income-tax (Amendment) Act of 1939 was passed.

2. *Facts of the Case.*—The assessee is a Hindu undivided family carrying on business in cloth, *sarrafa*, money-lending, grain, *arhat*, speculation in gold and silver, etc., at Rasra, Ballia and Calcutta. The assessee's accounts are maintained on the mercantile system with the

exception of those in respect of money-lending which are kept on the cash basis. The assessee in the preceding five years produced accounts purporting to have been properly closed, but for various reasons which it is unnecessary to mention here the book profits for those years were not accepted and the income of each of those years was computed for assessment purposes under the proviso to Section 13 of the Act. For the assessment year 1933-34 (the year with which we are now concerned and the "previous year" in respect of which was the account year ended Dasehra 1989), the assessee returned an income of Rs. 15,100, comprising Rs. 12,500 under "Business" and Rs. 2,600 under "Property." The details of the business income, shown at the round figure of Rs. 12,500, were not furnished; nor did the accounts, submitted in compliance with the notice under Section 22 (4), support this figure exactly. The Income-tax Officer held that the accounts had been so kept that the correct income could not be deduced therefrom. Consequently, acting under the proviso to Section 13 of the Act, he determined the business income at Rs. 28,766 by applying various percentage rates to the turnover disclosed by the goods accounts in certain sets of accounts. Adding income of Rs. 3,500 for property and Rs. 223 for dividends, he made the assessment on a total income of Rs. 32,489. A copy of the Income-tax Officer's assessment order, dated the 27th March, 1934, is appended as Exhibit A.

The assessee appealed against this assessment. In the course of the appellate proceedings, the Assistant Commissioner, after examining the account books, found that no details of cash sales were given in the books and that the various items of deposits in the personal accounts had not been properly investigated by the Income-tax Officer. The Assistant Commissioner, therefore, remanded the case to the Income-tax Officer with directions that he should prepare Trial Balance Sheets in respect of each set of accounts and should call upon the assessee to explain from what sources the items shown as deposits in the personal accounts had been received. A copy of the Assistant Commissioner's remand order, dated the 29th November, 1934, is appended as Exhibit B. The assessee, however, expressed his inability to furnish the information required and asked to be allowed to withdraw his appeal. (A copy of the Income-tax Officer's remand report, dated the 11th April, 1935, is appended as Exhibit C). The Assistant Commissioner refused to permit the withdrawal of the appeal as he thought that there were grounds for supposing that there had been under-assessment; and he accordingly had a notice served upon the assessee requiring him to show cause why the assessment should not be enhanced by treating as profits the deposits in the personal accounts. The assessee showed cause and

adduced evidence; but the explanation offered was not accepted by the Assistant Commissioner, who then himself examined the assessee's accounts in greater detail and found that the deposits in the personal accounts were not capital receipts but were profits which by a process of manipulation had been introduced into the books of accounts in the guise of capital receipts. He, therefore, came to the conclusion that the proper method of determining the profits was not to apply standard rates to the turnover shown in the various goods accounts but to add the net accretion of capital to the profit shown in the profit and loss accounts. As a result of substitution of this method of computation for that adopted by the Income-tax Officer the assessable income was found to be Rs. 51,842. The total income was thus enhanced by the Assistant Commissioner by Rs. 19,353 from Rs. 32,489 to Rs. 51,842. A penalty of Rs. 5,000 was also imposed under Section 28 of the Act. Copies of the Assistant Commissioner's orders enhancing the assessment and imposing the penalty are appended as Exhibits D and E respectively.

The assessee thereupon preferred two appeals under Section 32 of the Act to the then Commissioner of Income-tax (Rai Bahadur K. P. Verma) who, for the reasons detailed in his order, dated the 28th March, 1937 (a copy of which is appended as Exhibit F), reduced the addition of Rs. 19,353 by half and directed that the penalty be also reduced proportionately. In conformity with this order, the total income was fixed at Rs. 42,166 and penalty at Rs. 3,895.

The assessee then filed an application, dated the 24th May, 1937, under Section 66 (2) of the Act, asking my predecessor to refer certain alleged questions of law to the High Court for decision. A copy of this application is appended as Exhibit G. My predecessor, however, refused to refer the case to the High Court as, in his opinion, no question of law arose from his order under Section 32 of the Act. A copy of my predecessor's order, dated the 1st September, 1937, is appended as Exhibit H.

It was in these circumstances that the assessee moved your Lordships under Section 66 (3) of the Act and your Lordships have now been pleased to direct me to state a case and to refer the question of law, as set out in paragraph 3 below, for your Lordships' decision. A copy of your Lordships' order is appended as Exhibit J.

3. *Question of law.*—The question of law which I have been directed to refer to your Lordships is as follows:

“Whether the Assistant Commissioner had jurisdiction in appeal to substitute a different method of computation for the method which had been adopted by the Income-tax Officer?”

This question is accordingly referred to your Lordships for decision under Section 66 (3) of the Act.

4. *Commissioner's Opinion*.—A point very similar to that involved in this case was decided by your Lordships in *In re Pearey Lal Shukla*¹ a few days after the present order under Section 66 (3) of the Act was passed. In that case the Income-tax Officer had computed the assessable profits, under the proviso to Section 13, at a flat rate of 16 per cent. In appeal the Assistant Commissioner enhanced the assessment by increasing the rate of profit to 26·7 per cent. and in second appeal this rate was reduced by the Commissioner to 18 per cent., which was still higher than the rate taken by the Income-tax Officer. The question of law referred to your Lordships was “Whether, under the circumstances of the case, the Assistant Commissioner and Commissioner had authority under the law to change the basis of profit from 16 per cent. as calculated by the Income-tax Officer to any higher percentage?” Your Lordships answered this question in the affirmative and in doing so your Lordships relied on certain observations of the Privy Council in the case of *Commissioner of Income-tax, Bihar and Orissa v. Maharajahdhiraja Kameshwar Singh of Darbhanga*² and remarked that those observations were clear authority for the proposition that the basis and manner of assessment applied by the Income-tax Officer can be set aside in appeal by the Assistant Commissioner under Section 31 (3) (b) of the Act. It is true that in the present case the Assistant Commissioner enhanced the assessment, not by increasing the rates of profit applied by the Income-tax Officer, but by substituting a different method of computation; but this does not, in my respectful opinion, make any difference. It is clear, that under the wide discretion vested in the Income-tax Officer by the proviso to Section 13 of the Act, it was open to him in the circumstances of the case to adopt any basis and manner of computation he thought fit and that, instead of the flat rate basis, he could himself have employed the method of computation adopted by the Assistant Commissioner in appeal. It follows that, under the equally wide powers given to the Assistant Commissioner by Section 31 (3) of the Act in respect to any order of assessment, he could legally substitute a method of computation which, in his opinion, should have been adopted by the Income-tax Officer for that which he thought had been wrongly applied. This is clear from the following passage in the judgment of the Privy Council quoted by your Lordships in the case referred to above:

“The fact that the Income-tax Officer has justifiably proceeded on a basis and in a manner of his own in computing the assessee's income,

(1) (1942) 10 I.T.R. 239.

(2) (1933) 1 I.T.R. 94.

profits and gains does not, of course, exempt his computation from examination on appeal and, if it appears that he has adopted a wrong method, the assessment may be set aside."

As your Lordships were pleased to remark in *Pearey Lal Shukla's case*¹, there is nothing in the Act to restrict in respect to an assessment made under the proviso to Section 13 the powers which the higher authorities of the Department have under Sections 31 and 32 in respect to assessments generally.

For these reasons I submit that the question of law referred in this case should be answered in the affirmative.

5. As required by the prescribed rules, a copy of the draft statement of facts and question of law was sent to the assessee for any additions or amendments he might like to suggest. In his reply, without date but received in this office on the 4th August, 1942, the assessee disputed the correctness of the statement of facts in one respect. The statement has been modified accordingly in this respect. A copy of the assessee's reply is appended as Exhibit K."

The High Court (Collister and Bajpai, JJ.,) delivered the following judgment:

JUDGMENT.

In compliance with our order dated the 11th of February 1942 the Commissioner of Income-tax, Central and United Provinces, has stated a case and referred a question of law for our decision. We indicated that question of law in our order, and the same question has been referred to us for decision by the learned Commissioner. The question is as follows:—

"Whether the Assistant Commissioner had jurisdiction in appeal to substitute a different method of computation for the method which had been adopted by the Income-tax Officer?"

Under the provisions of Section 66 (3) of the Act if the Commissioner has refused to state a case on the ground that no question of law arises and the assessee makes an application to this Court, then if we are satisfied that a question of law does arise (it may be a substantial question of law or otherwise) we can require the Commissioner to state a case and to refer the question of law that does arise for our decision.

It was under these circumstances that we directed the Commissioner to state a case, but now that all the facts have come out on a perusal of the various orders of the Income-tax authorities, we think that the question of law in the circumstances of the present case ought to be answered in the affirmative.

The facts are that the assessee is a Hindu undivided family which carries on business in cloth, *sarrafa*, money-lending, grain, *arahaat*

speculation in gold and silver etc. etc. at Rasra, Ballia and Calcutta. The assessee owns as many as six shops in these places and when the profits for the year 1933-34 were being assessed the Income-tax Officer looked into the accounts of all these six branches and came to the conclusion that the profits were Rs. 32,489/-. In some of the branches the Income-tax Officer calculated the profits on the books filed by the assessee himself, and he thought that there it was possible to determine the profits after a reference to the books of account. As regards two or three branches he was of the opinion that some profits could be calculated with reference to the books of account but some other profits ought to be added inasmuch as the books of account did not afford sufficient data for calculating the profits, and in respect of certain turnover the Income-tax Officer under the proviso to Section 13 of the Act computed the profits in such manner as he thought best and he held the view that a certain standard rate of profit on the sales should be adopted. In this manner he calculated the profits of the various branches and came to the conclusion that Rs. 32,489/- were the profits of the assessee for the year 1933-34.

There was an appeal to the Assistant Commissioner and in the first instance the Assistant Commissioner asked for a report from the Income-tax Officer. It is true that the Assistant Commissioner uses the word "remand" which ordinarily under the Civil Procedure Code is considered, as it were, a final order of the appellate authority passed after the disposal of the case, but in this particular instance it is quite clear from the order of the Assistant Commissioner dated the 19th November 1934 that all that the Assistant Commissioner did was to ask for a report from the Income-tax Officer. This, we think, he was entitled to do under the provisions of Section 31 (2) of the Act.

When the Income-tax Officer was submitting a report, the assessee did not co-operate with him but wanted to withdraw the appeal and therefore the Income-tax Officer on the 11th April 1935 submitted a more or less colourless report saying that no explanation has been offered regarding deposits in personal accounts. The Assistant Commissioner then on the 17th of December 1936 considered the appeal on the merits. He also looked into the accounts of the various branches and in the end he agreed with the method of calculation adopted by the Income-tax Officer to a certain extent. He said that the income determined by the Income-tax Officer was Rs. 32,489/- but this income was made up not only of the profits shown in the various shops but also included certain income calculated by the application of flat rates on the turnover. He was of the opinion that that was not a proper method of calculating the profits and he, therefore, deducted the

amount which was obtained by the application of flat rates. This latter income was Rs. 11,884/-. From Rs. 32,489/- he deducted Rs. 11,884/- and a sum of Rs. 171/- as bad debt and found the income of the assessee to be Rs. 20,434/-, but where the Income-tax Officer had calculated the profits in certain instances on the basis of flat rate, the Assistant Commissioner was of the opinion that the income could be determined by a reference to the books of account themselves, and it was not necessary to adopt any flat rate at all. Certain income was shown as capital deposits and the Assistant Commissioner held the view that these deposits were really profits and therefore a sum of Rs. 31,408/- ought to be added to Rs. 20,434/-. The total income was determined at Rs. 51,842/.

We are not very much concerned with what the Commissioner did in appeal, but we may mention here that considering all the circumstances of the case he thought that profits disguised as deposits were not Rs. 31,408/- but only half of them. To that extent relief was granted by the Commissioner.

The question which we have got to decide is whether under the circumstances of this case the Assistant Commissioner had the power in certain matters arising in the present case to set aside the flat rate adopted by the Income-tax Officer and to determine the profits from the account books themselves. We think that there is nothing in the Act which would prevent the Assistant Commissioner from doing so.

It is contended that the proviso to Section 13 bars the Assistant Commissioner from doing what he has done in the present case. We, however, think that the language of the proviso does not afford support for the contention that his basis or his method of computation is not liable to interference by the higher authorities of the Department. It is true that the assessee cannot, as a matter of right, question the basis of computation and the manner of computation adopted by the Income-tax Officer if the latter feels that the method of accounting employed by the assessee is such that the income, profits and gains of the assessee cannot be properly deduced therefrom. But the words in Section 31 (2) (a) of the Act are very wide, and as we said in the case of *Commissioner of Income-tax v. Pyare Lal Shukla*¹ there is nothing in the Act to restrict, in respect to an assessment made under the proviso to Section 13, the powers which the higher authorities of the Department have under Sections 31 and 32 in respect to assessments generally. Learned Counsel for the assessee did not in so many words dispute the position taken by the Department that the powers of the Assistant Commissioner were very wide under the provisions of

(1) (1942) A.L.J. 388 ; 10 I.T.R. 239.

Section 31 of the Act, but what he said was that the powers should be exercised by the Assistant Commissioner himself, and he contended that when the Assistant Commissioner remanded the case on the 29th of November 1934 he took the case out of his own file and directed the Income-tax Officer to arrive at a decision different from what he had arrived at on an earlier occasion. As we pointed out before, the learned Assistant Commissioner had not on the 29th of November 1934 taken out the case from his own file but had only asked for a report from the Income-tax Officer and this he was entitled to do under Section 31 (2) of the Act. When the matter came finally before him after the report of the Income-tax Officer he was entitled under Section 31 (3) either to confirm or to reduce or to enhance the assessment. He chose to do the latter and his powers are not in any way circumscribed by the Act.

For the reasons given above, we answer the question referred to us in the affirmative, and we direct the Registrar to send a copy of our judgment under the seal of the court to the Commissioner. Learned counsel for the Department is entitled to the costs of the reference which we assess at Rs. 150/-.

Reference answered in the affirmative.

[IN THE MADRAS HIGH COURT].

AL. VR. V. P. PETHAPERUMAL CHETTIAR

v.

COMMISSIONER OF INCOME-TAX, MADRAS.

SIR LIONEL LEACH, C. J., and LAKSHMANA RAO, J.

August 27, 1948.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 2 (1) (a), 4 (3) (viii)—
AGRICULTURAL INCOME—RENT—INTEREST ON ARREARS OF RENT
PAYABLE UNDER MADRAS ESTATES LAND ACT—WHETHER AGRICUL-
TURAL INCOME.

Interest on arrears of rent payable by a ryot to a landholder under Section 61 of the Madras Estates Land Act is not agricultural income within the meaning of Section 2 (1) (a) of the Income-tax Act. It is neither 'rent' nor 'revenue' derived from land. It is an additional sum payable to the landholder as a compensation for the delay in the payment of the rent and its source is the tenant's default in the performance of his contract.

In re Manager, Radhika Mohan Roy Wards Estate [1940] (8 I.T.R. 460); *Maharaj Bahadur Ram Ran Vijay Prasad Singh v. The Province of Bihar* [1942] (I.L.R. 21 Pat. 488; 10 I.T.R. 446) Approved;

Sri Ramachandra Dev v. Commissioner of Income-tax, Bihar and Orissa [1942] (I.T.R. 21 Pat. 461; 10 I.L.R. 141) Not approved.

Commissioner of Income-tax, Madras v. Zamindar of Kirlampudi (I.L.R. 55 Mad. 830) explained.

Case referred to the Madras High Court by the Income-tax Appellate Tribunal, Calcutta Bench, under Section 66 (1) of the Indian Income-tax Act, 1922 (XI of 1922) as amended by Section 92 of the Indian Income-tax (Amendment) Act, 1939 (VII of 1939) in Reference 66 R. A. No. 1 Madras of 1942-43 on its file for decision on the following questions of law, namely,

(i) whether the amount received by the appellant as interest on preference shares from the Steel Corporation of Bengal, is a capital receipt?

(ii) whether the interest on rent payable to the appellant as landholder under the Madras Estates Land Act can be said to be agricultural income within the meaning of Section 2 (1) (a) of the Act and so exempt from assessment under Section 4 (3) (viii) of the Income-tax Act?

Case Referred No. 10 of 1943.

On the application of the assessee under Section 66 (1) of the Income-tax Act, the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. VERMA, (Judicial Member) and P. N. S. AIYAR (Accountant Member) referred the case to the Madras High Court on 9th December 1942 :—

STATEMENT OF CASE.

“This is an application for reference preferred by one Mr. AL. VR. V. P. Pethaperumal Chettiar, asking us to refer to the High Court the following questions of law said to arise from the order passed by this Bench of the Tribunal on 31st January 1942 in Appeal R.A.A. No. 36 Madras of 1941-42 :—

(i) Whether on the facts set forth above the dividend in question is assessable as income under the Indian Income-tax Act, 1922, as amended by Act VII of 1939?

(ii) Whether the sum of Rs. 574-8-0 in question is not an allowable expenditure under Section 10 (2) of the Act?

(iii) Whether when the interest realised from ryots by the appellant (who is a landholder) in virtue of the provisions of the Madras Estates Land Act is rent under that Act, such rent is not agricultural income exempt from assessment within the meaning of Section 4 (3) (viii) read with Section 2 (1) (a) of the Income-tax Act?

2 The Commissioner of Income-tax, Madras, who is the respondent in this case, has replied that the case does not raise points of law

Section 31 of the Act, but what he said was that the powers should be exercised by the Assistant Commissioner himself, and he contended that when the Assistant Commissioner remanded the case on the 29th of November 1934 he took the case out of his own file and directed the Income-tax Officer to arrive at a decision different from what he had arrived at on an earlier occasion. As we pointed out before, the learned Assistant Commissioner had not on the 29th of November 1934 taken out the case from his own file but had only asked for a report from the Income-tax Officer and this he was entitled to do under Section 31 (2) of the Act. When the matter came finally before him after the report of the Income-tax Officer he was entitled under Section 31 (3) either to confirm or to reduce or to enhance the assessment. He chose to do the latter and his powers are not in any way circumscribed by the Act.

For the reasons given above, we answer the question referred to us in the affirmative, and we direct the Registrar to send a copy of our judgment under the seal of the court to the Commissioner. Learned counsel for the Department is entitled to the costs of the reference which we assess at Rs. 150/-.

Reference answered in the affirmative.

[IN THE MADRAS HIGH COURT].

AL. VR. V. P. PETHAPERUMAL CHETTIAR

v.

COMMISSIONER OF INCOME-TAX, MADRAS.

SIR LIONEL LEACH, C. J., and LAKSHMANA RAO, J.

August 27, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 2 (1) (a), 4 (3) (viii)—
AGRICULTURAL INCOME—RENT—INTEREST ON ARREARS OF RENT
PAYABLE UNDER MADRAS ESTATES LAND ACT—WHETHER AGRICULTURAL INCOME.

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In re Manager, Radhika Mohan Roy Wards Estate [1940] (8 I.T.R. 460); *Maharaj Bahadur Ram Ran Vijay Prasad Singh v. The Province of Bihar* [1942] (I.L.R. 21 Pat. 488; 10 I.T.R. 446) Approved;

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(i) whether the amount received by the appellant as interest on preference shares from the Steel Corporation of Bengal, is a capital receipt?

(ii) whether the interest on rent payable to the appellant as landholder under the Madras Estates Land Act can be said to be agricultural income within the meaning of Section 2 (1) (a) of the Act and so exempt from assessment under Section 4 (3) (viii) of the Income-tax Act?

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(i) Whether on the facts set forth above the dividend in question is assessable as income under the Indian Income-tax Act, 1922, as amended by Act VII of 1939?

(ii) Whether the sum of Rs. 574-8-0 in question is not an allowable expenditure under Section 10 (2) of the Act?

(iii) Whether when the interest realised from ryots by the appellant (who is a landholder) in virtue of the provisions of the Madras Estates Land Act is rent under that Act, such rent is not agricultural income exempt from assessment within the meaning of Section 4 (3) (viii) read with Section 2 (1) (a) of the Income-tax Act?

2 The Commissioner of Income-tax, Madras, who is the respondent in this case, has replied that the case does not raise points of law

falling under Section 66 (1) of the Income-tax Act to justify a reference to the High Court and has proceeded in his reply to say that the questions on dividends, income and interest realised from ryots have been concluded by decided cases. The reply of the respondent does not seem to us to negative the contention that the questions raised are questions of law.

3. The Commissioner of Income-tax has, however, in his reply, proceeded to state the following three questions as the questions to be referred if the Tribunal decides to make a reference to the High Court:—

(i) Whether the amount received by the appellant as interest on preference shares from the Steel Corporation of Bengal is a capital receipt?

(ii) Whether the sum of Rs. 574-8-0 paid as interest is an allowable item for deduction under Section 10 (2) (xii) of the Act?

(iii) Whether the interest on rent payable to the appellant as landholder under the Madras Estates Land Act can be said to be agricultural income within the meaning of Section 2 (1) (a) of the Act and so exempt from assessment under Section 4 (3) (viii) of the Act?

The applicant has no objection to the questions being stated in the form mentioned by the Commissioner of Income-tax and we proceed to state the case.

4. The applicant received a payment from Steel Corporation of Bengal as interest on his capital and it was contended that actually the payment was not any dividend from the profits of the company but was interest paid by the company out of its capital and as such it was a capital receipt in the hands of the share-holder. The item in respect of which this contention was raised was only a sum of Rs. 160 and at the time when the claim was made before the Income-tax Officer the prescribed certificate under Section 20 of the Income-tax Act was not produced. The applicant, however, filed that certificate dated 1st December 1939, for the sum of Rs. 80 only before the Appellate Assistant Commissioner. This certificate showed that the sum that was paid was interest on preference shares and that it was paid out of the capital and no income-tax was deducted at source. Ordinarily the companies deduct income-tax before distributing dividends out of profits but in this case it was not so deducted as the disbursement was interest on the capital paid during a construction. No doubt it was paid out of the capital as there were no profits available to the company. This payment of the company was within its powers under Section 107 of the Indian Companies Act. This Bench of the Tribunal took the view

that this sum was paid as interest and tax was rightly levied on this as income received by the applicant. The contention in regard to the balance of Rs. 80, we merely rejected, holding that the total sum of Rs. 160 was not exempt from the liability to pay tax.

5. The Commissioner of Income-tax has submitted in regard to this point that the question decided by the Tribunal has been concluded by the decision of the House of Lords in *Williamson v. Ough*¹.

6. The second of the points decided by this Bench of the Tribunal in its order, dated 31st January 1942, in appeal R.A.A. No. 36 Madras of 1941-42 was that the sum of Rs. 574-8-0 paid as interest to one M. V. R. M. Murugappa Chettiar was not an admissible deduction under Section 10 (2) (xii) of the Income-tax Act. The Tribunal found that this was not a business expense at all. "We consider that this is a pure question of fact and cannot legitimately be a subject-matter of reference.

7. The third question of the applicant is in regard to the contention that the sum of Rs. 794 realised as interest on arrears of rent from the tenants of the Zemindari was not assessable to income-tax. This Bench of the Tribunal held that the interest on arrears of rent is not agricultural income and is thus liable to attract income-tax. This Bench of the Tribunal relied on the case of *Manager, Radhika Mohan Roy Wards Estate*, reported in 1940 I.T.R. 460 and came to the conclusion that the interest on arrears of rent is not agricultural income and is liable to tax. The applicant has drawn the distinction that in virtue of Section 61 of the Madras Estates Land Act the term "rent" includes also interest payable under Section 61.

Section 61 of the Madras Estates Land Act is as under :—

"Subject to the provisions of this Act, an arrear of rent shall bear simple interest at the rate of one-half per centum per mensem from the date on which the arrear fell due until it is liquidated."

All that the above section says is that the arrears of rent shall bear simple interest. Interest, however, is paid for failure to pay the rent in due time and is not either agricultural income as per the definition of agricultural income given in the Income-tax Act nor is it a proceed of land. It is merely a payment as damages for wrongful detention of money and therefore was taken to be liable to pay income tax.

8. Having decided that the application raises some questions of law we proceed to refer the following two questions of law to the High Court of Judicature at Madras for their opinion with slight modifications in question No. (iii) as formulated by the Commissioner of Income-tax and do not refer the second of the questions raised by the parties:—

(1) (1936) 20 Tax Cas. 194 ; 4 I.T.R. Suppl. 1.

Questions of law referred :

(i) Whether the amount received by the appellant as interest on preference shares from the Steel Corporation of Bengal is a capital receipt ?

(ii) Whether the interest on rent payable to the appellant as landholder under the Madras Estates Land Act can be said to be agricultural income within the meaning of Section 2 (1) (a) of the Act and so exempt from assessment under Section 4 (3) (viii) of the Income-tax Act ?

9. The papers mentioned in the index attached will form the paper book in this case."

On the question whether interest on arrears of rent is agricultural income, the opinion of the Appellate Tribunal as stated in the Judgment of the Tribunal delivered under Section 38 of the Act was as follows:—

"No. III—*Zemindari Income—Rs. 715.*—The appellant is earning interest of the sum of Rs. 715 as arrears of rent. The appellant contends that interest on arrears of land rent is agricultural income within the meaning of Section 2 (i) (a) and is exempt under Section 4 (3) (viii) of the Income-tax Act. He has argued before us that the case of the *Manager, Radhika Mohan Roy Wards Estate*¹ is distinguishable on the wording of the two Acts. He argues, two definitions in the two Provincial Acts differ and this should not be deemed to be conclusive. We have heard the representative of the appellant and are unable to agree with him on the distinction which he has drawn out. His arguments may be summarised as under: Madras Estates Land Act defines rent in Section 3, Clause (11), as:—

"Rent means whatever is lawfully payable in money or in kind or in both to a landholder for the use or occupation of land in his estate for the purpose of agriculture, and includes whatever is payable on account of the use and enjoyment of water supplied or taken for cultivation of land where the charge for such water has not been consolidated with the rent payable for the land."

Sections 60 and 61 of the said Act were produced to bring out his argument. He argues that the interest paid on arrears of rent is a lawful payment to a landholder for the use or occupation of the land for the purpose of agriculture and, therefore, is agricultural income. It may be pointed out (*sic*) in the Act although we do not agree with the exposition of law as propounded by the appellant's representative. We are concerned with the interpretation of the word 'agriculture' in the Income-tax Act, and the modifications, if any, in the Provincial Acts will not make any difference. Section 2, clause (1), defines agricultural income as under:—

(1) (1940) 8 I.T.R. 460.

"Any rent or revenue derived from land which is used for agricultural purposes, and is either assessed to land revenue in British India or subject to a local rate assessed and collected by officers of the Crown as such."

In order that income may be exempt, it is necessary that it should be land revenue derived from land.

Interest is a liability which a person incurs for non-payment in due time but interest cannot be said to be an agricultural income. It is something which a man pays for wrongful retention of the sum of money which is lawfully payable to a landlord. Agricultural income literally means income from or appertaining to agriculture. The learned Judges of the Calcutta High Court have devoted their learned attention to this matter and we respectfully follow the ruling. Interest paid is a sort of statutory recompense to the landlord and it cannot be said to be agricultural income within the meaning of the Income-tax Act. We, therefore, negative the claim of the appellant for the allowance.

5. The result is that the appeal is dismissed and the assessment order is confirmed."

K. V. Sessa Ayyangar, for the Commissioner.

V. V. Srinivasa Ayyangar, for the assessee.

JUDGMENT.

(The judgment of the Court was delivered by the Honourable the Chief Justice.)

Two questions have been referred to this Court by the Income-tax Appellate Tribunal, Calcutta Bench, at the request of the assessee. Mr. Srinivasa Ayyangar, on behalf of the assessee, has informed the Court that his client does not wish to proceed with the reference so far as it concerns the first matter. This means that the decision of the Tribunal on the question of whether the interest received by the assessee in respect of the preference shares held by him in the Steel Corporation of Bengal is taxable income will stand.

The second question reads as follows:

"Whether the interest on rent payable to the appellant as landholder under the Madras Estates Land Act can be said to be agricultural income within the meaning of Section 2 (1) (a) of the Act and so exempt from assessment under Section 4 (3) (viii) of the Income-tax Act."

The assessee is a landholder within the meaning of the Madras Estates Land Act. Section 61 of the Act states that an arrear of rent payable by a ryot to his landholder shall bear simple interest at the rate of one-half per cent. per mensem from the date on which the arrear fell due

until it is liquidated. The Income-tax Officer held that the interest which the assessee received from his tenants under this section is not agricultural income within the meaning of Section 2 (1) of the Indian Income-tax Act, 1922, and therefore he was liable to pay the tax on it. It is true that until the decision of the Calcutta High Court in *In re Manager, Radhika Mohan Roy Wards Estate*¹ the Department regarded interest paid on arrears of rent of agricultural land as being agricultural income. The former practice does not, however, preclude the Income-tax authorities from maintaining that they were wrong and that such income is taxable. In this case the Appellate Tribunal held that the assessee had been lawfully assessed in this respect.

The term "agricultural income" is defined in Section 2 (1) of the Income-tax Act. The term includes any rent or revenue derived from land which is used for agricultural purposes, and is either assessed to land revenue in British India or subject to a local rate assessed and collected by officers of the Crown as such, and any income derived from such land by agriculture.

In *In re Manager, Radhika Mohan Roy Wards Estate*¹ the Calcutta High Court had to consider whether interest on arrears of rent payable under the Bengal Tenancy Act was rent or revenue derived from land. So far as this case is concerned there is no difference between the Bengal Tenancy Act and the Madras Estates Land Act. The Calcutta High Court held that interest on arrears of rent was not agricultural income. It was pointed out that rent is payable to the landlord by the tenant by virtue of a contract of tenancy of land and the cause of action in respect of rent arises out of contract. Interest on arrears of rent is payable by reason of a statutory provision of law which "imposes a penalty upon the tenant for non-payment of his rent." The Patna High Court followed this decision in *Maharaja Bahadur Ram Ran Vijay Prasad Singh v. The Province of Bihar*² although in an earlier case, *Sri Ramachandra Dev v. The Commissioner of Income tax, Bihar and Orissa*,³ it expressed a contrary opinion. The earlier case was a reference under the Income-tax Act and the later case a reference under the Bihar Agricultural Income-tax Act, 1938, but we can see no reason for a distinction.

In our judgment, interest on arrears of rent payable by a ryot to the landholder under the Madras Estates Land Act is not agricultural income within the meaning of the Income-tax Act. Such interest is not rent. It is an additional sum payable to the landholder as compensation for the delay in the payment of the rent. Nor can it be classified as revenue "derived" from the land. Its source is the tenant's

(1) (1940) 8 I.T.R. 460

(3) (1942) I.L.R. 21 Pat. 461; 10 I.T.R. 141,

(2) (1942) I.L.R. 21 Pat. 488; 10 I.T.R. 446.

default in the performance of his contract. It is true that under the Madras Estates Land Act the landholder may distrain for arrears of rent and interest thereon, but that does not make the arrears rent. Section 3 (11) of that Act defines "rent" as meaning:

"Whatever is lawfully payable in money or in kind or in both to a landholder by a ryot for the use or occupation of land for the purpose of agriculture and includes whatever is lawfully payable on account of water supplied by the landholder or taken without his permission for cultivation of land where the charge for water has not been consolidated with the charge for the use or occupation of the land."

Section 5 of the Madras Estates Land Act makes the rent and the interest a first charge on the land but again we do not consider that this alters the character of the interest. In deciding whether interest is or is not agricultural income within the meaning of the Income-tax Act, the Court can only have regard to the definition contained in that Act.

Our attention has been drawn to the judgment of the Special Bench of this Court which decided *Commissioner of Income-tax, Madras v. Zamindar of Kirlampudi*¹. It was there held that interest due to a zamindar under a promissory note taken by him from his ryots for the amount of rent due by them with interest was not agricultural income within the meaning of the Income-tax Act. The basis of the decision was that there was a fresh contract between the zamindar and the ryots whereby the character of the liability was changed. It was no longer rent but a loan. Apparently it was contended in that case that interest on arrears of rent must be regarded as agricultural income by reason of Section 61 of the Act, but the Bench did not hold that interest on arrears of rent was agricultural income. It has been suggested that there is indication in the judgment that the Bench was of this opinion. It is certainly open to doubt whether the judgment is indicative of this, but even if it were, the judgment is not binding on us because the question did not arise in that case.

The present case was rightly decided by the Income-tax Tribunal and our answer to the second question referred is that interest on rent payable to the appellant is not agricultural income within the meaning of Section 2 (1) (a) of the Income-tax Act.

The assessee has lost on the question argued and he must pay the costs, Rs. 250/-.

Reference answered accordingly.

(1) I.L.R. 55 Mad. 830.

[IN THE MADRAS HIGH COURT.]

O. RM. OM. RM. PL. MUTHUKARUPPAN CHETTIAR & OTHERS

v.

COMMISSIONER OF INCOME-TAX, MADRAS.

SIR LIONEL LEACH, C. J., and LAKSHMANA RAO, J.

August 18, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 10, 24—LOSS—PARTNERSHIP—WINDING-UP—LOSS INCURRED IN REALIZATION OF ASSETS—WHETHER ALLOWABLE.

A firm carrying on a money-lending business was dissolved on the 11th January 1939 and after the dissolution no business was transacted beyond that involved in the realization of the assets. Between that date and the 26th March 1939, the assets of the business were realized. The assessee who was a partner in the firm claimed in relation to the year of account ending on 13th April 1939 that a certain amount representing the loss arrived at by deducting the sums realized in the course of the winding-up from the value of the assets as shown in the books of account should be deducted from his assessable income :

Held, that the alleged loss cannot for purposes of tax be treated as a trading loss in the year of account since the firm ceased to carry on business on the 11th January and all realizations took place after that date, and that, as the loss incurred was not incurred either in or for the carrying on of the business of the partnership, it was not an admissible deduction.

Income-tax Commissioner v. Shaw Wallace and Co. [1932] (59 I.A. 206 ; I.L.R. 59 Cal. 1343) and Wilson Box (Foreign Rights) Ltd., (In Liquidation) v. Brice (H. M. Inspector of Taxes) [1936] (20 Tax Cas. 736) referred to.

Cases stated under Section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, in pursuance of the High Court's order dated 24-8-1942: O. P. Nos. 126, 127 and 128 of 1942.

STATEMENT OF CASE.

(O. P. No. 126 of 1942).

"In accordance with the High Court's order referred to above, I have the honour to refer the question set out in paragraph 7 below for the decision of the Hon'ble Judges of the High Court under Section 66 (3) of the Indian Income-tax Act, 1922 (XI of 1922), before the Amendment on 1st April 1939 (hereinafter referred to as the Act).

2. For the tax year 1939-40 (previous year, Tamil year Bahudanya ended 13th April 1939) the petitioner was assessed by the

Income-tax Officer, Devakottah, on a total income of Rs. 19,999/-(19,057/- reduced on appeal). This included *inter alia* his share of income in a partnership concern at Penang called O. R.M. OM. Penang and a sub-partnership known as OM. P. S. which had a one-fourth share in every loan lent by O. R.M. OM. In arriving at the income from these businesses the Income-tax Officer had disallowed among others the following items claimed by the petitioner as deductions :

O. R.M. OM. Penang :

(a) \$ 120,489·88—loss on sale of assets to the partners on the winding-up of the firm.

(b) \$ 3,684·20—loss on sale of shares to partners on the winding-up of the firm.

(c) \$ 35,100—amount written off in the accounts of the debtors, being the difference between the amount due and the values for which the debts were sold to the partners on the winding-up of the firm.

OM. P. S. Penang :

(a) \$ 37,454·79—loss on the sale of assets to the partners on the winding-up of the firm.

(b) \$ 1,128·06—loss on the sale of shares to the partners on the winding-up of the firm.

(c) \$ 11,700—amount written off in debtors' accounts being the difference between the amount due and the value for which the debts were sold to the partners on the winding-up of the firm.

The above figures also included a loss of \$ 13,017 arising by the sale of certain assets of the main partnership business O. R.M. OM., and a loss of \$ 4,339 arising by the sale of certain assets of the sub-partnership OM. P. S., to S.P.S. Shanmugham Chettiar, a partner in the sub-partnership business OM. P. S.

3. The facts relating to these items are as follows :—

O. R.M. OM., partnership concern—items (a), (b) and (c):—This firm which carried on money-lending business consisted of four partners including the petitioner who had 7 annas share in the business. The firm, like many other Chettiar firms, held lands, gardens and houses which, it would appear, were taken over from debtors in the course of its business. For the assessment in question its 'previous year' was the year 13-4-38 to 13-4-39. The partners decided to discontinue the business of the firm and dissolve the partnership as on 11-1-39. Except one item of property sold to a stranger at a loss of \$ 2,346 all the other properties, 28 in number, were sold on 26th March 1929 to the partners at the market price which was less than the cost price. The difference between the cost price of the assets and the value fixed for the purpose of their sale to the partners was claimed as a loss to be set off against

the income under other heads. Such difference amounted to \$ 120,489·88. Besides, some of the debts due to the firm were sold to the partners at a loss of \$ 35,100. The partners took over also some of the shares (companies) belonging to the firm and the result of this transfer of shares was also a loss of \$ 3,684·20 to the firm. Taking into account the above three items of losses the partners in the firm claimed a loss of \$ 138,349·44 in the firm. The Income-tax Officer disallowed the claim. He observed that the firm had not been valuing the profit or loss in the books and that therefore any loss arising in the year of account out of the depreciation in the value of the properties could not be claimed as a deduction from the firm's profits.

*Sub-partnership OM. P. S. Penang—Items (a), (b) and (c) :—*This firm consisted of the following partners:—

- (1) S. P. S. Shanmugam Chettiar,
- (2) O. RM. OM. Firm referred to above, and
- (3) P. R. S. Alagappa Chettiar.

The method of business of this firm was such that it had no standing independent of the main firm O. RM. OM., so that when O. RM. OM., was wound up these two had necessarily to be wound up. It was wound up in the same manner as the main firm. The assets consisting of immovable properties and loans were sold to the partners. This resulted in a loss to the petitioner as in the case of the main firm. The Income-tax Officer disallowed the losses, holding that they were of the same nature as the losses of the main firm.

4. *Loss on sale of certain assets of O. RM. O. M. to S. P. S. Shanmugam Chettiar :—*Some of the assets of the two firms were sold to S. P. S. Shanmugam Chettiar who had half share in the OM. P. S. firm. The loss on the sale of such assets was \$ 17,356 made up of \$ 13,017 included in \$ 120,489 and \$ 4,339 included in \$ 37,454 referred to in paragraph 2 above. It was contended that so far as \$ 13,017 was concerned it could not be said that it arose out of any sale or a distribution of assets among partners. The Income-tax Officer did not accept this claim, stating that the loss was exactly similar to the loss arising from the sale of the other properties in the course of winding-up of the business. An extract of the Income-tax Officer's order is filed, marked Exhibit A.

5. The petitioner's appeal to the Appellate Assistant Commissioner was unsuccessful. An extract of his order is filed, marked Exhibit B.

6. The petitioner then filed an application under Section 66 (2) of the Act and requested my predecessor to refer to the High Court

certain alleged questions of law. My predecessor declined to do so, on the ground that no questions of law arose for decision. A copy of his order is filed, marked Exhibit C.

7. The petitioner then moved the High Court under Section 66 (3) of the Act and the High Court has by its order dated 24th August 1942 directed me to state a case and refer the following question of law, which I accordingly refer for the decision of the Hon'ble Judges of the High Court.

"Is the loss claimed by the assessee in this case of a capital nature or is it a loss deductible in the year of account?"

8. Under Section 10 (1) of the Act, "the tax shall be payable by an assessee under the head profits and gains of business, profession or vocation in respect of the profits or gains of any business, profession or vocation *carried on* by him." In order to answer the question submitted for decision it is necessary to find out whether the losses were trading losses arising from a business *carried on* by the firm or not. It is not disputed that the sales of the assets of the business including the debts, on account of which the losses arose were effected for the purpose of winding up the business and distribution of the assets. It cannot be contended that the winding-up in this case involved the carrying on of any part of the trade. As a matter of fact the firm stood dissolved on the 11th January 1939 and the sale of the assets comprising a large number of items valued at more than 4 lakhs (28 landed properties valued at about Rs. 4 lakhs, shares in companies valued at \$ 24,523 and certain number of inams) was put through as a single transaction on the 26th March 1939. It was exclusively a case of the realisation of the assets without involving the carrying on of a trade. The sale of a firm's assets in the winding-up of the firm cannot be said to be a trading transaction. The loss arising as a result of such activities is not therefore a trading loss but only a capital loss. Had there been any profit to the firm in the sale of the assets in question, it could not have been liable to payment of income-tax. It follows therefore that where the sale of the assets of a firm as part of the winding-up of the business results in a loss, no deduction in respect of that loss can be claimed by the assessee. In this view the question of the loss being in the year of account does not arise. But if the loss should be held to be a trading loss in respect of a business carried on by the assessee it will be deductible in the year of account. I respectfully submit that this question should be answered accordingly."

[In O. P. Nos. 127 and 128 of 1942 the facts were the same as in O. P. No. 126 of 1942—Ed.]

M. Subbaraya Iyer, for the assessee.

K. V. Sessa Ayyangar, for the Commissioner.

JUDGMENT.

(Judgment of the Court was delivered by the Honourable the Chief Justice.)

The assessee was a partner in a firm carrying on a money-lending business at Penang under the style of O. R.M. OM. and as such had an interest in the business of a sub-partnership trading under the style of OM. PS. The business of the sub-partnership was also carried on at Penang. The firm of O. R.M. OM. was dissolved on the 11th January 1939 and between that date and the 26th March 1939 the assets of the business were realised. After the 11th January 1939 no business was transacted beyond that involved in the realization of the assets. One of the assets was sold to a stranger; all the other assets were sold to members of the firm. The winding-up of the O. R.M. OM. partnership meant, of course, the winding-up of the subsidiary partnership as well.

This reference relates to the year of account which ended on the 13th April 1939. The assessee claims that in assessing his income as a partner in these businesses an aggregate sum of \$ 1,38,349 should be treated as representing trading loss. This figure is arrived at by deducting the sums realized in the course of the winding-up from the values of the assets as shown in the books of account.

By an order dated the 24th August 1942 this Court directed the Commissioner of Income-tax to state a case on the following question :

“Is the loss claimed by the assessee in this case of a capital nature or is it a loss deductible in the year of account?”

The question was stated in this way as the Court understood that the case of the Income-tax authorities was that the loss should be treated as being of a capital nature.

It is quite clear that the alleged loss cannot for purposes of tax be treated as a trading loss in the year of account, because the firm ceased to carry on business on the 11th January 1939 and all realizations took place after that date. Section 10 (1) of the Income-tax Act states that the tax shall be payable by an assessee under the head “profits and gains of business, profession or vocation” in respect of the profits or gains of a business “carried on” by him. The importance of the words “carried on” was pointed out by the Privy Council in *Income-tax Commissioner v. Shaw Wallace & Co.*¹ Their Lordships also pointed out that the English cases did not help here in the interpretation of the Indian Act which was not *in pari materia*. But this does not preclude the Court from referring to English cases when deciding whether a loss incurred in the course of the liquidation of a business can be regarded

(1) (1932) 59 I.A. 206 ; 59 Cal. 1343.

as a trading loss. In *Wilson Box (Foreign Rights) Ltd. (In Liquidation) v. Brice (H. M. Inspector of Taxes)*¹, it was held that a profit made in the winding-up of a company was not assessable to income-tax. The profit was not made in carrying on the business of the company, but in its liquidation. Lawrence, J., said that the liquidator of a company might realize the assets of the company without carrying on the business of the company in such a way as to attract income-tax. On the other hand, the liquidator might realise the assets in such a way as to involve the carrying on of a trade, the profits of which would be assessable to income-tax. This decision was upheld by the Court of Appeal.

If a profit made in the course of the liquidation of a business does not represent taxable income it must follow that a loss suffered in realization is not a deductible loss. Of course, just as in the case of a company, the business of a dissolved partnership may be carried on in order to facilitate the winding-up of the partnership and if a profit is made it will be taxable as such. Likewise a loss will be a deductible loss. But in this case the business was not "carried on." It stopped completely on the 11th January 1939, after which the partners contented themselves with taking steps to realize the assets. As the loss incurred was not incurred either in or for the carrying on of the business of the partnership it is not deductible under Section 10. The reference will be answered in this sense.

The Commissioner of Income-tax is entitled to his costs which we fix at Rs. 250.

O. P. No. 127 of 1942.

The facts are the same as the facts in O. P. No. 126 of 1942 which we have just decided and the answer given there is the answer which we give to the question referred in this case.

The Commissioner is entitled to his costs which we fix at Rs. 150.

O. P. No. 128 of 1942.

The facts are the same as the facts in O. P. No. 126 of 1942 which we have just decided and the answer given there is the answer which we give to the question referred in this case.

The Commissioner is entitled to his costs which we fix at Rs. 150.

Reference answered accordingly.

[IN THE CALCUTTA HIGH COURT.]

KUMAR DEBA PROSAD GARGA AND OTHERS

v.

COMMISSIONER OF INCOME-TAX, BENGAL.

SIR HAROLD DERBYSHIRE, C. J., and GENTLE, J.

June 17, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 2 (1) (a)—AGRICULTURAL INCOME—INTEREST ON ARREARS OF RENT REALISED UNDER SEC. 67, BENGAL TENANCY ACT—WHETHER AGRICULTURAL INCOME—WHETHER TAXABLE.

Income arising from interest on arrears of rent under Section 67 of the Bengal Tenancy Act is not agricultural income within the meaning of Section 2 (1) (a) of the Income-tax Act and is therefore taxable.

In re Manager Radhika Mohan Roy Wards Estate [1940] (8 I.T.R. 460) followed.

Cases referred to :

Manager Radhika Mohan Roy Wards Estate, *In re* [1940] (8 I.T.R. 460).

Maharaja Bahadur Ram Ran Vijay Prasad Singh v. Province of Bihar [1942] (10 I.T.R. 446).

Case stated to the Calcutta High Court under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by the Indian Income-tax (Amendment) Act, 1939, by the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. VARMA (Judicial Member) and P. N. S. Aiyar (Accountant Member) for the decision of the question mentioned in para. 4 of the Statement of Case : (No. 4 of 1942).

STATEMENT OF CASE.

“The applicant, in this case, has asked for a reference of the following questions of law to the High Court at Calcutta :—

(i) Whether in the circumstances of the case the Kumars should not have been individually assessed for interest on securities,

(ii) Whether the sum of Rs. 36,810 was taxable in the facts of the case,

(iii) Whether in the facts and circumstances of the case the disallowance of the management expenses was legal, and

(iv) Whether the addition on estimate of Rs. 1,500 to the income already shown under the head ‘Non-agricultural homestead lands’ was legal ?

The respondent, the Commissioner of Income-tax, Bengal, has filed his reply stating that—

Question (i)—does not arise out of the appellate order.

The Tribunal did not deal with this point as they held that it had not been held before the Income-tax Officer and the appellant's counsel conceded the matter ;

Question (ii)—is a question of law and is covered by the decision of the Calcutta High Court in the case of *Radhika Mohan Roy Wards Estate*¹ ;

Question (iii)—is alleged not to arise out of the order of the Tribunal ; and

Question (iv)—is not a question of law.

2. The applicant, at the time of the hearing before us, conceded that the objections raised by the respondent are right in regard to the questions (i), (iii) and (iv). Question (ii) is pre-eminently a question of law and although it is covered by the authority of the Calcutta High Court, we think that the applicant is entitled to have the reference on this question, the question being one of law. We, therefore, proceed to state the case for the opinion of the High Court at Calcutta.

3. The applicant is a big Zamindar and besides rent has income from interest or damages on the arrears of rent. The sum, in this case, claimed is Rs. 36,810 as being the income arising from the interest on arrears of rent or damages awarded to the applicant. The contention of the applicant before the Income-tax Officer that this interest on arrears of rent is agricultural income was repelled. This Bench of the Income-tax Appellate Tribunal also took the same view following the case of *Manager, Radhika Mohan Roy Wards Estate, In re*, a case decided by the Calcutta High Court and reported in [1940] (8 I.T.R. 460). On the interpretation of this ruling this Bench of the Income-tax Appellate Tribunal came to the conclusion that the effect of this ruling has covered general cases. The distinction drawn by the learned counsel of the appellant who argued before us in appeal R.A.A.No. 34-Bengal of 1941-42 that this ruling of the Calcutta High Court is based on some other cases, the facts of which were distinguishable, did not find favour with us. The Tribunal held that the ruling was binding on it and gave effect to it.

4. *Question of law*.—The question that now arises for the opinion of the High Court is :—

“Whether the interest or damages recovered under Section 67 of the Bengal Tenancy Act in respect of the arrears of rent is agricultural income ? ”

We, therefore, refer the following question of law to the High Court at Calcutta :—

(1) (1940) 8 I.T.R. 460.

“ Whether the sum of Rs. 36,810 representing the income arising from interest on arrears of rent under Section 67 of the Bengal Tenancy Act is a taxable income or not ? ”

Manindra Nath Ghosh, for the assessee.

P. B. Chakravartthi and *J. C. Pal*, for the Commissioner.

JUDGMENT.

DERBYSHIRE, C. J.—In my opinion the question of law arising in this case was decided by a Division Bench of this Court on July 3, 1940, in the case of *In re Manager Radhika Mohan Roy Wards Estate*—a Reference under the provisions of Section 66 of the Indian Income-tax Act—reported in [1940] (8 I.T.R. 460). That case has been followed ever since not only by this Court but by the High Court at Patna in the case of *Maharaja Bahadur Ram Ran Vijay Prasad Singh v. Province of Bihar* [1942] (10 I.T.R. 446) which was decided on April 1, 1942, by a Bench consisting of Harries, C. J., Fazl Ali and Manohar Lal, JJ.

At page 456 of the report Harries, C. J., referring to the case of *In re Manager Radhika Mohan Roy Wards Estate* observed: “ In my view, there is no doubt whatsoever as to the correctness of this decision that interest on arrears of rent is not rent. ”

There is only one answer to the question put in the present case—it is that the sum of Rs. 36,810 representing the income arising from interest on arrears of rent under Section 67 of the Bengal Tenancy Act is taxable income. In my view the law is perfectly clear and if an assessee under these circumstances comes here and asks for a decision we can only refer him to these cases and order that he pays the costs of the reference.

The result is that the sum of Rs. 36,810 representing the income arising from interest on arrears of rent under Section 67 of the Bengal Tenancy Act is taxable income. The assessee who brought this question must pay the costs of this Reference which are assessed at eleven gold mohurs. This will include the costs of preparing the paper book.

GENTLE, J.—I agree.

Reference answered accordingly.

[IN THE CALCUTTA HIGH COURT.]

MESSRS. SURPAT SINGH DUGAR AND OTHERS

v.

COMMISSIONER OF INCOME-TAX, BENGAL

SIR HAROLD DERBYSHIRE, C.J., and GENTLE, J.

June 17, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 66 (1)—REFERENCE—
ACADEMIC QUESTION—PRACTICE OF HIGH COURT.

In a reference under Section 66 (1) of the Indian Income-tax Act, the High Court will not answer a question which is purely of an academic nature.

Raja Bahadur Sir Rajendra Narayan Bhanja Deo v. Commissioner of Income-tax, Bihar and Orissa [1940] (8 I.T.R. 495; A.I.R. 1940 P.C. 158) followed.

Case stated under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by the Indian Income-tax (Amendment) Act, 1939, by the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. VARMA (Judicial member) and P. N. S. AIYAR (Accountant Member) for the decision of the question mentioned in para 7 of the Statement of Case : (No. 3 of 1942).

STATEMENT OF CASE.

“The applicant by his application filed on the 16th March 1942, has asked us to refer the following question of law to the High Court at Calcutta :—

“Whether in the facts and circumstances of the case the proceedings started by the learned Income-tax Officer under Section 34 for the assessment year 1938-39 were legal?”

The respondent, the Commissioner of Income tax, Bengal, was called to file his reply which he has done and he has formulated the following question as the one arising from the facts of the case. The applicant also agrees that this is the only question of law to be referred :—

“Whether in the facts and circumstances of the case the action of the Income-tax Officer in issuing a notice under Section 34 for the assessment year 1938-39 was valid in law?”

2. The question that arose for determination by the Tribunal was whether Section 34 of the Income-tax Act was rightly applied in the circumstances of this case.

3. The facts are that the appellants are a firm consisting of three partners each one representing a 'Hindu Undivided Family.' These three families were assessed up to the assessment for the year 1935-36 as separate entities. In the assessment for the year 1935-36 the three families were clubbed together as an "Association of Individuals." This term was used before the present amendment for the "Association of Persons." The assessment was made on them on their entire income consisting of the incomes from :—

- (i) Interest on securities,
- (ii) Income from property,
- (iii) Dividends and other sources, and
- (iv) Business.

In respect of the assessments on them for the years 1936-37 and 1937-38 as an 'Association of Individuals', they protested on question of status and contended that they could not be regarded as "Association of Individuals." The matter was taken by the applicants before the Commissioner of Income-tax, Bengal, under Section 33 of the Indian Income-tax Act. Before this matter could be decided by the Commissioner of Income-tax, Bengal, the assessments for the year 1938-39 was made as before by the Income-tax Officer on the three persons as an 'Association of Individuals' on the 15th February, 1939. Thus, for the three years 1936-37, 1937-38 and 1938-39 assessments had been made on the three persons as an 'Association of Individuals. The Commissioner of Income-tax, Bengal, by his order dated the 12th May, 1939, accepted the contention in respect of the assessment for the year 1936-37 that the three families ought not to be clubbed together. The assessments for 1936-37 and 1937-38 had, therefore, to be made afresh on the basis of that order. This order of the Commissioner of Income-tax, Bengal, was duly intimated to the Income-tax Officer, who had, on the 15th February, 1939, already made the assessment for the year 1938-39.

4. On the 6th March, 1939, an appeal had been preferred to the Appellate Assistant Commissioner in regard to the assessment made for the year 1938-39. In view of the Commissioner's order referred to above and in view of the pendency of the appeal against the assessment for the year 1938-39 the Income-tax Officer apprehended that the assessment made by him was, in all likelihood, to be modified and would be cancelled. The Income-tax Officer, therefore, thought that if timely action was not taken by him the result would be that the income in respect of the year 1938-39 would escape in the hands of various persons constituting the 'Association of Individuals' in case

the appeal was accepted which was bound to be in view of the order of the Commissioner of Income-tax in the case of earlier year.

5. The Income-tax Officer considered that an assessment would have to be made in respect of interest on securities, income from properties and other sources in the hands of the three families separately and another one to be made on the three families as a firm in respect of the income from 'Business' carried on by them together. After the receipt of the order of the Commissioner of Income-tax, Bengal, in respect of the assessment for the year 1936-37 on the 14th July, 1939, the Income-tax Officer served a notice on the firm (appellants) under Section 34 of the Income-tax Act requiring it to furnish a return of its income for the assessment for the year 1938-39 on the ground that such income had escaped assessment in the year 1938-39 in its hands. It is the validity of this notice that the applicants contend now.

6. For reasons stated in our order dated the 12th January 1942 in appeal R. A. A. No. 39—Bengal of 1941-42, we held that Section 34 of the Income-tax Act was applicable to the facts of the case with the result that the assessment was confirmed.

7. *Question of law.*—The question being purely of law we have no hesitation in referring it to the High Court. We, therefore, refer the following question as formulated by the respondent, Commissioner of Income-tax, Bengal, to the High Court at Calcutta for its opinion :—

“Whether in the facts and circumstances of the case the action of the Income-tax Officer in issuing a notice under Section 34 for the assessment year 1938-39 was valid in law?”

Manindra Nath Ghosh, for the assessee.

P. B. Chakravarthi and J. C. Pal, for the Commissioner.

JUDGMENT.

GENTLE, J.—The applicant is a firm consisting of three partners each of whom is also the Karta of a Hindu undivided family. Up to and including the year 1934-35 the three families were each separately assessed to income-tax. In the year 1935-36 they were grouped together and were assessed as an association of individuals. The assessment contained the whole of the income of the three families from all sources including the profits from the business conducted by the applicant firm. In the years 1936-37 and 1937-38 similar assessments were made as in the previous year. The assessee objected, in respect of these two assessments, to the method by which they had been made, the objection being taken to the Commissioner of Income-tax who took cognizance of the matter under Section 33 of the Indian Income-tax Act.

Whilst these two assessments were under consideration by the Commissioner, the Income-tax Officer on February 15, 1939, made a further assessment upon the association of individuals for the year 1938-39 and against which an appeal was preferred to the Appellate Assistant Commissioner on March 6, 1939. By his order dated May 12, 1939, the Commissioner accepted the contention that the three families should not have been grouped together in one assessment and the profits of the firm should be eliminated from it. The Commissioner's order was passed after the Income-tax Officer had made the assessment upon the association for the year 1938-39 and before the appeal against it was decided.

On July 14, 1939, the Income-tax Officer was informed of the Commissioner's order and he served a notice under Section 34 of the Act upon the applicant firm requiring it to furnish a return of profits from the business for assessment for the year 1938-39 on the ground that they had escaped assessment for that year.

On July 5, 1940, the appeal by the association in respect of the assessment made upon it for the year 1938-39 was allowed and on December 21, 1940, the applicant firm was assessed in respect of the year 1938-39 under Sections 23 (3) and 34 of the Act.

The validity of the notice under Section 34 of the Act is questioned in this Reference. The question which is raised is "Whether in the facts and circumstances of the case the action of the Income-tax Officer in issuing a notice under Section 34 for the assessment year 1938-39 was valid in law?"

During the course of the argument it transpired that the association has paid all the tax pursuant to the assessment for the years 1936-37 and 1937-38 and that the firm has also paid the tax in respect of the year 1938-39. The individuals who were the subjects of the assessment upon the association and upon the firm are in fact the same. The learned Advocate on behalf of the applicants stated that whatever may be the answer to the question raised in this Reference, whether it is in favour of the applicant firm or whether it is adverse to it, there will be no action taken to obtain refund of any of the income-tax which has in fact been paid. The payments which have been made will remain and the assessments have all been fully satisfied so far as tax is concerned.

The question raised is one which can never recur so far as the applicant firm or the association are concerned. That being so, it seems that the question is one to which the answer would be purely academic and nothing else; no purpose would be served by answering the question; and nothing would follow from the answer which might be

given. In *Raja Bahadur Sir Rajendra Narayan Bhanja Deo v. Commissioner of Income-tax, Bihar and Orissa*¹, the position in regard to academic questions in income-tax reference was considered and discussed by the Judicial Committee. In the course of the judgment of the Board delivered by Luxmoore, L.J., he pointed out that the question referred to the High Court for its consideration in that matter had only an academic interest whichever way it might be answered. Later the learned Lord Justice observed that in those circumstances their Lordships did not think it would be right to depart from the well-established practice of the Board to refuse to decide a question which was purely academic, and later still, that in their Lordships' opinion, both the respondent and the High Court ought to have refused to answer the question referred to it.

On the authority of the decision, to which reference has just been made, this question being purely of an academic nature this Court is not called upon nor required in any way to express any opinion by giving an answer to the question. The result is that this Reference will be returned.

DERBYSHIRE, C. J.—I agree.

Reference returned.

[IN THE LAHORE HIGH COURT.]

MESSRS. SEHGAL BROTHERS, *In re*.

DIN MOHAMMAD and MARTEN, JJ.

June 3, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEOS. 30, 42, 43—APPEAL—
NON-RESIDENT—ORDER APPOINTING PERSON AS AGENT OF NON-RESIDENT—WHETHER APPEALABLE.

Under Section 30 of the Income-tax Act, 1922, an appeal does not lie against the order of an Income-tax Officer appointing a person an agent of a non-resident company under Section 43, where neither the non-resident company nor the person appointed agent has been assessed in respect of profits accruing to the company in British India from its connection with the person appointed as agent.

Gokul Das Chunilal v. Commissioner of Income-tax [1932] (A.I.R. 1932 Nag. 152) distinguished.

Case stated under Section 66 (1) of the Indian Income-tax Act, 1922 (XI of 1922) as amended by Section 92 of the Indian Income-tax (Amendment) Act, 1939 (VII of 1939) by the Income-tax Appellate

(1) (1940) 8 I.T.R. 495; A.I.R. 1940 P.C. 158.

Tribunal, Delhi Bench, consisting of YAHYA ALI, (President) and A. L. SAHGAL (Accountant Member) for the decision of the question of law mentioned in para 7 of the Statement of Case :

Civil Reference No. 13 of 1942.

STATEMENT OF CASE.

“ 1. This is an application by Messrs. Sehgal Bros. of Jullundur under Section 66 (1), Income-tax Act, 1922, requiring us to state to the High Court of Judicature at Lahore certain questions which it is claimed, are questions of law and arise out of our order dated the 20th March, 1942, in Miscellaneous Appeal No. 1 (Punjab) of 1940-41.

2. The applicants are the sole selling agents, with their headquarters at Jullundur, of Messrs. Jagajit Sugar Mills Co. Ltd., a company carrying on the business of manufacture of sugar at Phagwara in the Kapurthala State. It is common ground that this company is not resident in British India within the meaning of clause (c) of Section 4A, Income-tax Act. The manner in which business is co-ordinated between the Company and Sehgal Bros, is described by the Income-tax Officer from personal knowledge as follows :—

“ Purchasers enter into agreement with the agents at Jullundur City, who get confirmation from the Phagwara company on telephone. Goods are sent by the company by rail and the railway receipt, which is generally in favour of self, is passed on to the selling agents, who endorse it in favour of the purchasers. Money realised is credited by the agents into the account of the company in the local branch of the Imperial Bank.”

3. On the 11th March, 1942, the Income-tax Officer served on Messrs. Sehgal Bros. a notice under Section 43, Income-tax Act, requiring them to show cause within a week of the receipt of the notice why they should not be treated for the assessment years 1938-39 and 1939-40 as agent of the non-resident Company which, according to his information, was in receipt of income, profits and gains in British India through them. Messrs. Sehgal Bros. did not choose to appear and show cause before the Income-tax Officer, with the result that the Income-tax Officer recorded an order under Section 43 of the Act declaring Messrs. Sehgal Bros. agents of the Company for the assessment years 1938-39 and 1939-40. The profits accruing or arising to the Company in British India have not as yet been assessed for the year 1938-39 or for the year 1939-40.

4. Messrs. Sehgal Bros. appealed to the Appellate Assistant Commissioner from the order of the Income-tax Officer appointing them as agents under Section 43 (1). The Appellate Assistant Commissioner

held that the assessment of the non-resident Company in respect of profits accruing in British India not having been completed, no appeal lay from that order. From this order of the Appellate Assistant Commissioner, Messrs. Sehgal Bros. filed an appeal to the Tribunal and by our order dated 20th March 1942, we held that the view taken by the Appellate Assistant Commissioner was correct, and we dismissed the appeal. Messrs. Sehgal Bros. have now applied under Section 66 (1) requiring us to refer the following questions to the High Court of Judicature at Lahore :—

(a) Whether the Appellate Assistant Commissioner, Amritsar, and the Bench were not bound to follow the authority in *In re Gokal Das Chuni Lal v. Commissioner of Income-tax*¹ and hold that an appeal was competent and to entertain and decide the petitioner's appeal on merits in view of the principles of law laid down in Section 66 (5).

(b) That amendment having been made in law after the above decision which left this part of the statute without any amendment, it should be presumed that the Legislature accepted and adopted the interpretation placed by the Nagpur Court in the above ruling.

(c) And as to whether an appeal is not competent in the circumstances of this case.

5. The contention of the Commissioner of Income-tax in his reply filed under Rule 54 of the Appellate Tribunal Rules is that, as the assessment has not as yet been completed, no application under Section 66 (1) lies. As we find that our order under Section 33 gives rise to a question of law, we proceed to formulate it for the opinion of the High Court.

6. Our reasons for coming to the view that no appeal under Section 30 lies in such a case are given in our order of 20th March, 1942. None of the provisions in sub-section (2) of Section 30 dealing with the starting point of the period of limitation for different kinds of appeals is applicable to the present case. Further, the fact that the person "denying his liability to be assessed under this Act" under Section 30 is a person actually assessed is clear from sub-section (3) of Section 31, where the Appellate Assistant Commissioner's powers in the case of appeals from orders of assessment are detailed. None of the provisions of Section 31 which define the powers of the Appellate Assistant Commissioner to interfere in different kinds of appeals is applicable to an appeal of this kind.

7. We refer the following question of law for the opinion of the High Court :—

(1) (1932) A.I.R. 1932 Nag. 152.

Does an appeal lie under Section 30, Income-tax Act, 1922, against the order of an Income-tax Officer appointing a person an agent of a non-resident Company under Section 43 of the Income-tax Act, where neither the non-resident Company nor the person appointed agent has been assessed in respect of profits accruing to the Company in British India from its connection with the person appointed as agent?"

[The opinion of the Appellate Tribunal as stated in the Judgment of the Tribunal delivered under Section 33 of the Act was as follows].

"2. The order under appeal is canvassed on three grounds:—

(1) On the authority of the decision of the Court of the Judicial Commissioner, Nagpur, in *Gokal Das Chunilal v. Commissioner of Income-tax*¹.

(2) The principle that in view of the interpretation placed by the Court of the Judicial Commissioner, Nagpur, on the section, since no change was made in the relevant provision in the amended Act of 1939, it should be presumed that the legislature accepted and adopted the interpretation that was placed by the Court of the Judicial Commissioner, Nagpur, in the above ruling; and

(3) that the right of appeal should be deemed to have been conferred on the subject in the circumstances of this case.

3. We are not impressed by any of these grounds. The main question that came up for decision in the case of *Gokal Das Chuni Lal*¹ was whether the refusal by the appellate authority to entertain an appeal on the ground that no appeal lay was a question of law. Incidentally, however, the learned Judge observed that the clause "denying his liability to be assessed under this section is wide enough to cover the case of an assessee, who denies his liability to be declared an agent under Section 43 of the Act." That dictum is, to our minds, opposed to the general principle which has found expression in the judgment of Beaumont, C. J., in *Commissioner of Income-tax, Bombay v. Metro Goldwyn Mayer (India), Ltd.*², where his Lordship observed "Section 43 provides for the appointment by the Income-tax Officer of a statutory agent. But I think Section 43 is really only machinery for giving effect to Section 42, and the mere appointment of an agent under Section 43 would be of no consequence unless tax can be levied under Section 42." The phrase "denying his liability to be assessed under this Act" occurring in Section 30, in our view, distinctly points to a stage where the assessment has been made and it seems to us that the act of assessment must precede the liability to assessment. The right of appeal and reference to High Court can arise only if the liability to tax has been enforced.

(1) (1932) A.I.R. 1932 Nag. 152.

(2) (1939) 7 I.T.R. 176, at 184,

4. With reference to the second ground urged by the learned Counsel for the appellant, it is a matter of the intention of the legislature and we are satisfied that the legislature consciously refrained from providing the right of appeal against an order under Section 43, in view of the considerations that under the law an agent is competent to withhold out of any money payable by him to the non-resident person a sum equal to his estimated liability under the second proviso to Section 42 (1) and he has further the right to raise question of his liability in a regular appeal which he can prefer after the assessment has been made.

5. Lastly the right of appeal is not inherent in the subject but must be expressly conferred. It cannot be inferred by implication. There is no substance in any of the contentions put forward in this appeal and we concur in the view that no right of appeal has been provided under Section 30 against an order of appointment of an agent under Section 43.

6. The appeal is dismissed."

M. C. Mahajan, Kirpa Ram Bajaj and Mehta Amir Chand, for the assessee.

Raj Kishan, for the Commissioner.

The High Court (Din Mohammad and Marten, JJ.) delivered the following judgment:—

JUDGMENT.

This judgment will dispose of two cases which arise from orders made under Section 43 of the Indian Income-tax Act declaring the petitioners in each case agents in British India of certain firms doing business in State territory. In both cases appeals were lodged against these orders and were dismissed by the appellate authorities concerned as being premature, as no assessment of income-tax at that stage had been made. Applications were then made in each instance for a case to be stated in this Court. In the case of Messrs. Narang Brothers, the application was refused and this Court is now being asked to order that such a statement of the case should be made. In the second case, that of Messrs. Sehgal Brothers, the Income-tax Tribunal has stated the case to this Court and we are asked to adjudicate upon the following question:

"Does an appeal lie under Section 30, Income-tax Act, 1922, against the order of an Income-tax Officer appointing a person an agent of a non-resident Company under Section 43 of the Income-tax Act, where neither the non-resident Company nor the person appointed agent has been assessed in respect of profits accruing to the Company in British India from its connection with the person appointed as agent?"

On behalf of the petitioner it has been argued by Mr. Mehr Chand Mahajan that Section 30 of the Act gives a right of appeal to anyone denying his liability to be assessed under the Act. He points out that an order under Section 43 of the Act can, in accordance with the proviso, only be made after an opportunity has been given to the person affected thereby of being heard: therefore, an order under Section 43 declaring such a person to be an agent is an order passed after the parties concerned have been heard and the question has been adjudicated upon. He further points out that the effect of an order under Section 43 is automatically to make such an agent liable to assessment under Section 42 which provides that he shall be deemed to be for the purposes of this Act "the assessee." He relies on a judgment of the Nagpur High Court, *Gokul Das Chunilal v. Commissioner of Income-tax*, in which it was held that the scope of the words "denying his liability to be assessed" in Section 30, sub-section (1), is wide enough to cover the case of an assessee who denies his liability to be declared an agent under Section 43; therefore an appeal against the order of an Income-tax Officer under that section is not barred, though the appeal is not against the assessment itself.

It should, however, be noticed that the distinction between that case and the one now before us is that in the former, proceedings had advanced to the stage of assessment before the appeal was lodged, whereas in the present case there has not as yet been any assessment at all. The Nagpur judgment is, therefore, only an authority providing that once an assessment has been made the assessee can appeal against the order under Section 43 appointing him as agent, even though he does not actually appeal against the assessment. In the present case we are asked to go further and decide that an agent appointed under Section 43 can at once lodge an appeal against his appointment as such, before anything else is done to render him liable to payment of any income-tax. In our view it has been rightly decided that an appeal at this stage is premature.

The grounds given by the Income-tax Appellate Tribunal in support of its conclusion that no appeal lies at this stage are that none of the provisions of sub-section (2) of Section 30 which deal with the starting point of the period of limitation for different kinds of appeals is applicable in the present case. Further, Section 31 which provides the manner in which the Appellate Assistant Commissioner can exercise his powers in appeal, is not applicable to such an appeal as is now contemplated. We are of the view that the decision of the Income-tax Appellate Tribunal is correct.

In spite of the use of the word "assessee" in Section 42 we think it clear from a perusal of Sections 30 and 31 that the Legislature never contemplated such an appeal at this stage. The provisions contained in sub-section (2) of Section 30 of the old Act, which prescribe periods of limitation for appeals under various sections of that Act, have been considerably extended in the new Act. But still, no provision is made for any appeal against an order passed only under Section 43. Further, we do not see how the appellate authority could exercise any of its functions within the scope of sub-section (3) of Section 31 in deciding such an appeal. This seems to us to indicate clearly that the Legislature did not consider it necessary to provide an appeal against an order under Section 43 before any assessment had been attempted. The reason seems obvious. It does not necessarily follow that an agent nominated under Section 43 will ever actually be assessed. As already pointed out, if an assessment is made, the agent immediately has a right of appeal not only against the actual assessment but also, as found in the Nagpur case, against the order nominating him as agent.

Our answer to the question put in this reference is, therefore, in the negative. It follows that both these petitions must be dismissed with costs.

Reference answered in the negative.

[IN THE BOMBAY HIGH COURT.]

WALLACE BROS. & CO., LTD.

v.

COMMISSIONER OF INCOME-TAX, BOMBAY.

SIR JOHN BRAUMONT, C. J., and RAJADHYAKSHA, J.

July 22, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 4-A (c), 64—RESIDENCE OF COMPANY—FOREIGN COMPANY—PARTNER IN FIRM CARRYING ON BUSINESS IN BRITISH INDIA—INCOME OF COMPANY ARISING IN BRITISH INDIA EXCEEDING INCOME ARISING OUTSIDE BRITISH INDIA—STATUS OF COMPANY—WHOLE WORLD INCOME, WHETHER LIABLE TO TAXATION—SEC. 4-A (c), WHETHER *ultra vires*—INDIAN LEGISLATURE—POWER TO IMPOSE TAX ON INCOME ARISING OUTSIDE BRITISH INDIA—GOVERNMENT OF INDIA ACT, 1935, SECS. 99, 100.

The assessee was a company incorporated in the United Kingdom and the control and management of its affairs was situated wholly in that country. It was a sleeping partner in a firm which carried on, and had a place of, business in Bombay. In the year 1938-39 the

assessee made a profit of over seventeen lacs in British India as against a profit of about seven lacs in the United Kingdom. For the assessment year 1939-40, the Income-tax Officer for the area in which the firm was carrying on business treated the assessee as a resident under Section 4-A (c) of the Income-tax Act as amended by the Income-tax (Amendment) Act (VII of 1939) and assessed it on the whole world income. The assessee contended that Section 4-A (c) was ultra vires inasmuch as it was not within the extra-territorial powers conferred on the Indian Legislature by the Government of India Act, 1935 :

Held, (i) that Section 4-A (c) was not ultra vires the Indian Legislature and therefore the assessee was liable to be taxed on the whole world income ;

(ii) that the Income-tax Officer of the area in which the firm was carrying on business had jurisdiction to make the assessment under Section 64 (1) ;

(iii) that Section 4-A (c) (b) of the Amended Act was applicable to the assessment of the assessee for the year 1939-40.

BEAUMONT, C. J.—*As the power to impose income-tax is vested in the Indian Legislature, it has also the power to determine who is to pay the tax, and for that purpose to lay down rules as to who is to be regarded as resident in, and what income is to be deemed to arise in, British India.*

The mere fact that an Act of the Central Legislature has some extra-territorial operation is not enough to invalidate it. There is no provision in the Government of India Act which says that any extra-territorial legislation shall be outside the powers of the Indian Legislature.

Cases referred to ;

Colonial Gas Association Ltd. v. Federal Commissioner of Taxation (1934) 51 Commonwealth L.R. 172.

Egyptian Delta Land and Investment Co. v. Todd (1929) A.C. 1 ; 98 L.J.K.B. 1 ; 140 L.T. 50 ; 44 T.L.R. 747 ; 14 Tax Cas. 119.

Raleigh Investment Co., Ltd. v. Governor-General in Council (1943) 11 I.T.R. 393.

Swedish Central Railway Co. v. Thompson (1925) A.C. 495 ; 94 L.J.K.B. 527 ; 133 L.T. 97 ; 41 T.L.R. 585 ; 9 Tax Cas. 342.

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal, Bombay, for the decision of the questions mentioned in para. 10 of the Statement of Case : (Income-tax Reference No. 3 of 1948).

Under Section 38 of the Indian Income-tax Act (XI of 1922) the Income-tax Appellate Tribunal, Bombay, consisting of YAHYA ALI (President) and A. L. SAHGAL (Accountant Member) delivered the following judgment.

JUDGMENT OF APPELLATE TRIBUNAL.

"The appellants are Messrs. Wallace Bros. & Co. Ltd., a company which was incorporated in the United Kingdom and which has no Director in India. It is, however, a sleeping partner in the Bombay firm, Messrs. Wallace & Co. In years preceding the assessment year 1939-40, Messrs. Wallace & Co., were treated as agents of the British Company and assessed as such. In the year of charge the Income-tax Officer found that the income of the appellant Company arising in British India in the accounting year exceeded its income arising without British India in that year and treating the Company as a resident in British India within the meaning of Section 4-A (c), assessed it on its total income including that arising outside British India after making an allowance of Rs. 4,500 as income from outside not brought into British India. Before the Appellate Assistant Commissioner objections raised against the assessment were threefold :—

(1) that the business of the appellant company is directed and carried on, and the whole of its control and management abides, in London and that though it is a partner in the Bombay firm it does not carry on any business in British India;

(2) that Section 4-A (c) of the Indian Income-tax Act is *ultra vires* the Indian Legislature; and

(3) that Section 4-A could not be given retrospective effect so as to make the appellant firm resident in the previous year as the amending Act came into effect only as from 1st April, 1939.

All these contentions were negatived and hence this appeal. Before us, however, a further ground has been raised, *viz.*, that in the event of Wallace Bros. & Co. Ltd., being held to be residents, who are hit by the provisions of the Indian Income-tax Act, the assessment is nevertheless void since the provisions of Section 64 have not been complied with.

2. The income of the appellant firm arising in British India has been determined to amount to Rs. 17,85,831 and that arising outside British India has been found to be Rs. 7,43,927, the aggregate income thus being Rs. 25,29,758. These figures are not in dispute. *Ex concessis* its income arising in British India in the relevant accounting year exceeded its income arising without British India in that year and consequently sub-clause (b) of clause (c) of Section 4-A applies to the case, and in the absence of any paramount vitiating element such as the question of *ultra vires* raised in this matter, the British Company would be a resident in British India in the year preceding assessment year and would as such be liable under Section 4 (i) (b) (ii) to be assessed on its entire income accruing or arising to it both in and without

British India during that year. It is for this purpose that it has been strenuously contended that both Section 4-A (c) and Section 4 (i) (b) (ii) are *ultra vires* the Indian Legislature and the grounds urged in support of this plea are (a) that legislation of this character, which has the effect of altering the domicile of a company and of declaring a foreign company registered outside the country and having the whole of its control and management elsewhere to be a resident in this country, is not warranted by the provisions of Section 99 of the Government of India Act; (b) that such a provision is opposed to the canons of international law relating to the residence and domicile of trading corporations: and (c) that the legislation is vitiated on account of its being extra-territorial.

3. Before embarking upon an examination of these contentions, we have to note an objection traced *in limine* by the learned Advocate-General who appeared for the respondent, that this Tribunal, created as it is by the particular statute some of whose provisions are impugned as *ultra vires*, cannot go into that question but should on the other hand adopt the attitude assumed by the Income-tax Officer and the Appellate Assistant Commissioner that it was their function merely to administer the Act as it was and not to entertain questions relating to the validity of any of its provisions. When, however, it was pointed out that the powers, duties and functions of the Appellate Tribunal are judicial in nature and that for a final adjudication of the questions raised by the assessee by the High Court the only machinery existing is that of a reference through the Tribunal under Section 66 (1) of the Income-tax Act, the learned Advocate-General did not press his preliminary objection further.

4. Section 99 of the Government of India Act enacts *inter alia* that subject to the provisions of that Act, the Federal Legislature may make law for the whole or any part of British India. Under the transitory provision made in Section 316, the powers conferred on the Federal Legislature shall be exercisable by the Indian Legislature for the time being and until the establishment of the Federation. Section 100 (1) of the Act refers to List (1) of the Seventh Schedule to the Act and provides that the Federal Legislature has power to make laws with respect to any of the matters enumerated therein and item 54 of that List is "Taxes on income other than agricultural income." The question that falls to be decided is whether in enacting Sections 4-A (c) and 4 (1) (b) (ii), the Indian Legislature was not making a law concerning taxes on income for the whole or any part of British India. So far as Section 4-A (c) is concerned, what the Indian Legislature enacted was that in certain circumstances a foreign company would be deemed

to be a resident in British India in a particular year. The sub-clause (a) provided that it would be a resident if the control and management of its affairs are situated wholly in British India in that year. There can be no doubt about the correctness of that test as it is in strict conformity with the legislative trend and the current of judicial opinion in the United Kingdom. Sub-clause (b), with which alone we are concerned, contemplates the case of a foreign company which is carrying on trade or business in British India which causes income to arise in British India. It will be idle to contend that legislation of that kind covering trading corporation engaging in trade in the country is anything but legislation for the whole of British India. If then it is within the legislative competence of the Indian Parliament to make a law imposing tax on such incomes, it is equally within its power to determine the rate or incidence of such a tax and the principle embodied in sub-clause (b), providing the larger proportion of income made in British India as compared with that arising outside as the test of residence, is in the ultimate analysis a method of determining the rate or incidence of the tax. This acid test we have to apply to the case is whether the company was performing any acts or having any dealings which had the effect of yielding income in the taxing country, and if these premises are satisfied, there is scarcely any difficulty in holding that it was a law made for the whole of British India and as such *intra vires* the powers of the Indian Legislature. The mere fact that a portion of the income assessed arose or accrued outside British India does not, to our minds, make the provision incompetent. In this case although the appellant firm is incorporated in the United Kingdom, it is a partner in a firm in Bombay and has through that firm been carrying on business in this country and deriving income therefrom which is greatly in excess of the income that arose or accrued to it outside this country. The consideration that the appellant company is only a sleeping partner in the Bombay firm does not make the slightest difference. So long as the incorporated company is taxed by virtue of its having carried on business and earned profits here, it is legitimate to treat it as a resident in British India for the purpose of income-tax and there is no inherent impropriety or injustice in bringing such concerns within the pale of the fiscal statute. It must further be observed that if Section 4-A (c) is found to be *intra vires* as a law made for the whole of the British India, it would follow as an inevitable result that the legislature would be competent to make laws in any form it pleases affecting the residents in the country or those who have been duly declared under Section 4-A (c) to be residents in British India. The question of the constitutionality of Section 4 (i) (b) (ii) does not, therefore, arise for separate consideration.

5. The two remaining objections based on international law and extra-territorial character of the legislation do not call for elaborate treatment. The Courts in Great Britain are barred from entertaining an objection to the validity of an Act of Parliament on grounds such as these and on that analogy it would appear that the municipal courts in this country would also be incompetent to entertain an objection based on grounds of repugnance to international law. Secondly, the objection based on international law does not apparently fit in with the plea of *ultra vires*. Thirdly, "residence" is radically different from "domicile" and in this case the legislation in question does not, even in the remotest manner, affect the domicile of the British Company. So far as domicile is concerned, we are alive to the principle of the international law that it has to be at the place considered by the law to be the centre of its affairs which in the case of a trading corporation is its principal place of business, that is to say, the place where the administrative business of the corporation is carried on. But residence is not inherent in a company in the nature of things and "residence" for the purpose of taxation is a matter of express legislation which has to be determined by artificial rules. There is nothing contrary or repugnant to international law in enacting that the larger proportion of income made in British India as against that arising outside shall be the test of residence. A corporation may very well be considered resident in a country for one purpose and not for another as observed by Professor Dicey in "*Conflict of Laws*." As observed by Lord Loreburn, Lord Chancellor, in *De Beers Consolidated Mines Ltd. v. Howe*¹, residence of a company within the meaning of Income-tax Act is not necessarily the same thing as residence for the purpose of serving a writ. Again Viscount Cave, Lord Chancellor, pointed out in *Swedish Central Railway Co. Ltd. v. Thompson*², "The effect of this decision is that, when the central management and control of a company abides in a particular place, the company is held for the purposes of income-tax to have a residence in that place; but it does not follow that it cannot have a residence elsewhere. An individual may clearly have more than one residence (See *Cooper v. Cadwalader*³); and on principle there appears to be no reason why a company should not be in the same position." After reviewing exhaustively all the authorities, the Lord Chancellor stated on p. 505 of the report, "From the above examination it would appear that, while the authorities may not establish the possibility of a company having more than one residence for income-tax purposes, they are at least not inconsistent with that view.

(1) (1936) A.C. 455, at 460.

(3) (1904) 5 Tax Cas. 101.

(2) (1925) A.C. 495, at 501.

I do not cite the decisions as to the residence of a company for the purpose of founding jurisdiction, because they relate to a different subject matter ; but, so far as they go, they point to the same conclusion. I hold, therefore, that a company may, for income-tax purposes, have a residence here as well as a residence abroad." Lord Buckmaster, who was also a party to that decision, made the following observation : " The levying of tax is essentially a matter of domestic jurisdiction. A company may do such acts within the jurisdiction of this country as causes it to be liable here as resident to income-tax without excluding the possibility that it may also be held to be resident in another jurisdiction for the same or another purpose." (*Ibid* p. 519). The decision in *London & South American Investment Trust Ltd. v. British Tobacco Co., (Australia) Ltd.*, has no bearing on the facts of the present case as in that case there was no question of any business having been carried on in the taxing country. It is thus by no means clear that either the place of incorporation or the principal place of business or the place of its real control and management constitute exclusively the place of residence of a company for the purpose of the imposition of income-tax. It has been conceded in the various decisions bearing upon the point that for the purpose of income-tax a company may reside in more than one place and "residence" for the purpose of taxation is, as pointed out by Viscount Sumner in *Egyptian Delta & Land Co. v. Todd*¹, a matter for express legislation and not inherent in a company in the nature of things, as in the case of an individual. Quite apart from this aspect of the matter, it would be possible to countenance the view that even if the legislation in question tended to or had the effect of impinging upon the international law or was extra-territorial in its scope, the legislation would none the less be competent since the Indian Legislature has been held to have plenary powers of legislation as wide and extensive as the Parliament itself. It is hardly necessary to traverse the catena of decisions in which that principle has been propounded or applied, and we shall content ourselves with a brief reference to the dicta of the Privy Council in *Croft v. Dunphy*², in which while dealing with a case from the Dominion of Canada, Lord Macmillan said :

"In the well-known case of *Queen v. Burah*³, Lord Selborne in expressing the views of the Board in the comparable instance of India, uses this very significant language : 'The Indian Legislature has powers expressly limited by the Act of the Imperial Parliament which created it and it can of course do nothing beyond the limits which

(1) (1929) A.C. 1, at p. 11.

(2) (1933) A.C. 156.

(3) (1878) 3 A.C. 889.

circumscribe these powers, but when acting within those limits, it is not in any sense an agent or delegate of the Imperial Parliament but is and was intended to have plenary powers of legislation as large and of the same nature as those of Parliament itself."

Again on page 165 his Lordship observed :—

"The sole question is whether the Imperial Parliament in conferring upon Canada, as it admittedly has done, full power to enact customs legislation bestowed or withheld the power to enact the provisions now challenged. No question of any infraction of international law arises. The question is a domestic one between the Imperial Parliament and the Dominion Parliament."

It is not denied that the Parliament has unrestricted powers and its legislation would be valid notwithstanding that it may be contrary to or in conflict with international law, and it follows without any doubt that the Indian Legislature also has similar unrestricted and co-exhaustive powers to legislate on subjects allotted to it irrespective of whether the legislation is extra-territorial in nature and whether it is not in conformity with the principles of international law. We hold for the foregoing reasons that Sections 4-A (c) and 4 (i) (b) (ii) are not *ultra vires* the Indian Legislature and that consequently the Income-tax authorities were justified in treating the appellant company as a resident in British India within the meaning of Section 4-A (c) for the accounting year and in assessing the company on the aggregate income received both within and outside British India during that year.

6. The second objection is that Section 4-A (c) cannot be applied in respect of the previous year as it came into force on 1st April, 1939, and the previous year ended before that date. We had occasion to examine the entire case law bearing upon the point in R.A.A. No. 175, (Bombay) of 1941-42 (*Sir Cowasjee Jehangir, Second Baronet, Bombay v. Income-tax Officer, Bombay*), and, as a result of the investigation, we recorded our conclusion in the following passage :

"From the dicta of the various High Courts extracted above, it is manifest that it is not strictly speaking correct to characterise the application of Section 16 (1) (c) to the income of the previous year as amounting to giving retrospective effect but what is really done is to apply the principles in force in the year of assessment to the income of the previous year as computed under the provisions of the Act."

We are of the opinion that the same principle holds good with regard to the present case as well and that the Act as amended applies to the case as the assessment relates to the year 1939-40. This objection also fails.

7. The only question that remains is as to the alleged failure on the part of the Income-tax Officer to conform to the procedure prescribed in Section 64 of the Income-tax Act. Under the first clause of that section where an assessee carries on a business at any place, he shall be assessed by the Income-tax Officer of the area in which that place is situated. Under the second clause, in all other cases an assessee shall be assessed by the Income-tax Officer of the area in which he resides. It seems to us that both the clauses apply to the case. We have held that the assessee company was carrying on business in Bombay as the partner of Messrs. Wallace & Co. and they were, therefore, rightly assessed by the Income-tax Officer, Bombay. We have also found that the Company is a resident and since it is deemed to be a resident by reason of the larger proportion of its income having been earned in Bombay, it must be held that the Company is a resident in Bombay. In this view there is no substance in the objection that there was no Income-tax Officer who could assess a British Company whose principal place of business was in London.

8. The result is that the appeal fails and it is consequently dismissed."

On the application of the assessee under Section 66 (1) the Tribunal referred the case to the Bombay High Court:—

STATEMENT OF CASE.

"The Tribunal has been by this application required by the assessee, Messrs. Wallace Bros. & Co., Ltd. under Section 66 (1) of the Income-tax Act to refer to the High Court certain questions of law arising out of its order, dated 21-3-42, passed in R.A.A. No. 87—(Bombay) of 1941-42.

2. The assessee company was incorporated in the United Kingdom, and the control and management of its affairs is situated wholly in that country. The company has no Director in India, but it is a sleeping partner in the firm of Messrs. Wallace & Co., which, admittedly, carries on, and has a place of, business in Bombay. Until the assessment year 1939-40 the Bombay firm used to be treated for income-tax purposes and assessed to tax as agents of the British Company but in respect of the 1939-40 assessment the Company could be assessed without the interposition of an agent by virtue of the amended provisions of Section 42. On a scrutiny of the statements of accounts, dividend warrants, etc., furnished by the assessee its income arising in British India in the previous year was found finally by the Income-tax Officer to be Rs. 17,85,831 being made up as follows:—

| | |
|---------------------------------------------------------------------------------|--------------|
| (1) Share in the profits of the registered firm of Messrs. Wallace & Co. ... | Rs. 8,76,266 |
| (2) Share of dividends and interest received from the said firm ... | „ 18,197 |
| (3) Dividends ... | „ 8,59,428 |
| (4) Interest ... | „ 31,940 |
| | <hr/> |
| | „ 17,85,881 |

Its income accruing or arising without British India in the previous year was Rs. 7,48,427, consisting of:—

| | |
|---------------------------|--------------|
| Dividends ... | Rs. 8,23,040 |
| Less Loss in business ... | „ 74,613 |
| | <hr/> |
| | „ 7,48,427 |

The accuracy of these figures is not in dispute.

3. As the British Indian income admittedly exceeded the foreign income in the previous year the Income-tax Officer treated the Company as resident in British India having regard to the provision in sub-clause (b) of clause (c) of Section 4-A and on that footing included in the assessable income of the Company and assessed to income-tax and super-tax not only the income arising in British India under Section 4 (1) (b) (i) but also income accruing or arising to the Company without British India under Section 4 (i) (b) (ii) of the Act (less the allowance of Rs. 4,500). Objections raised by the assessee before the Income-tax Officer against the liability of its income from without British India to British Indian income-tax were negatived and the Appellate Assistant Commissioner also in appeal held the assessment of the said income by the Income-tax Officer to be in order and confirmed the same. Against the said appellate order the Company brought R.A.A. No. 87 (Bombay) of 1941-42 before the Tribunal and this reference arises out of the order in the said appeal whereby the Tribunal rejected the various contentions advanced by the assessee and dismissed the appeal.

4. As indicated in the Tribunal's order under Section 33, the objections raised against the assessment before the Income-tax authorities were:—

(i) That the business of the appellant company is directed and carried on, and the whole of its control and management abides, in London and though it is a partner in the Bombay firm it does not carry on any business in British India;

(ii) That Section 4-A (c) of the Indian Income-tax Act is *ultra vires* the Indian Legislature; and

(iii) That Section 4-A could not be given retrospective effect so as to make the appellant company resident in the previous year, as the Amending Act came into effect only as from the first April 1939.

5. With reference to the first and second contentions, the Tribunal found that so long as the income arising in British India in the relevant accounting year has in fact exceeded its income accruing or arising without British India in that year, the application of Sections 4-A (c) (b) and 4 (i) (b) (ii) cannot be resisted, except in the case of the operation of any paramount vitiating element, such as the question of *ultra vires* raised in this matter. As a matter of law, it was held for the reasons given in the order of the Tribunal that the aforementioned provisions of the Indian Income-tax Act were not *ultra vires* the Indian Legislature either in consequence of the legislative powers vested under the Government of India Act having been exceeded or on account of any repugnance to the canons of international law or usage concerning the residence and domicile of trading corporations or by reason of the alleged extra-territorial character of the legislation.

6. As regards the third objection, the Tribunal was of the view that Section 4-A of the Act as amended applied to the case as the assessment related to the year 1939-40, holding that it was not a question of giving any retrospective effect to the new provisions but it was a case of applying the principles in force in the year of assessment to the income of the previous year as computed under the provisions of the Act.

7. In the Memorandum of Appeal presented to the Tribunal a new point was taken by way of an alternative plea, to wit, that if the Company is deemed to be a resident within the provisions of Section 4-A (c) (b) it was not assessed by the Income-tax Officer of the area in which the place where the Company carried on its business is situate, Section 64 (1), or by the Income-tax Officer of the area in which the assessee resides, Section 64 (2), and that consequently the entire assessment is *ab initio* void. The Tribunal entertained this plea even though it was not raised before the Income-tax Authorities and held that both the clauses adverted to were duly satisfied. It was found that the assessee-company carried on its business during the accounting period in Bombay as the partner of Messrs. Wallace & Co. It was further found that by reason of the larger proportion of its total world income having been in actual fact earned in Bombay in the previous year the Company was resident in Bombay in that year. In that view it was decided that the Company was rightly assessed by the concerned Income-tax Officer—the Additional Income-tax Officer, Companies Circle, Bombay,—conformably to the requirements of Section 64.

8. The various questions formulated by the assessee for reference will appear from the Section 66 (1) application and the Memorandum

filed by him on 7-1-43 proposing a set of questions in substitution of those in the original application. The Commissioner of Income-tax, Bombay, in his reply filed under Rules 53 and 54 of the Appellate Tribunal Rules, while agreeing that certain questions of law arise from the order passed by the Tribunal, formulated four questions suggesting that the entire ground is effectively covered by them.

9. By the Memorandum, dated 7-1-43, referred to above, the assessee company sought permission to amend their Section 66 (1) application by substituting for the questions proposed in the original application a totally different set of questions wherein the aspect bearing on Section 64 has been greatly amplified. It would appear in particular from the fourth question—Part (B)—and sixth question—Parts (C) and (D)—that the contention is put forward for the first time at the belated stage that sub-section (2) of Section 64 and sub-clause (c) of Section 4-B are also *ultra vires* the Indian Legislature. These questions not having been propounded at all before the Tribunal at the appellate stage could not be, and were not, dealt with in its order under Section 33 and hence these are not matters which arise out of that order so as to form the subject-matter of a reference under Section 66 (1).

10. Upon the facts found by the Tribunal in this case we are of the opinion that the following questions of law arise and we accordingly refer the same to the High Court of Judicature at Bombay under Section 66 (1) of the Income-tax Act :—

(i) Whether in the circumstances found by the Tribunal in its order under Section 33 the assessee-company was taxable to income-tax and super-tax for the assessment year 1939-40 in respect of the income (Rs. 7,48,487 less Rs. 4,500) which accrued or arose to it without British India in the previous year?

(ii) Are the provisions of Sections 4-A (c) and 4 (1) (b) (ii) of the Income-tax Act *ultra vires* the Indian Legislature?

(iii) Is sub-section (b) of clause (c) of Section 4-A of the Amended Act applicable to the assessment of the assessee-company for the year 1939-40?

(iv) Whether on the facts found by the Tribunal the Additional Income-tax Officer, Companies Circle, Bombay, had jurisdiction under Section 64 (1) or Section 64 (2) to make the assessment?

Sir Jamshedji Kanga with *V. F. Taraporewala*, for the assessee.
M. C. Setalvad with *G. N. Joshi*, for the Commissioner.

JUDGMENT.

BRAUMONT, C. J.—This is a reference made by the Income-tax Appellate Tribunal raising four questions, but in substance only one

question calls for serious consideration, and that is whether the provisions of Section 4-A (c) of the Indian Income-tax Act, 1922, a sub-section introduced by the amending Act of 1939, are *ultra vires* in whole or in part. That sub-section provides that a company is resident in British India in any year (a) if the control and management of its affairs is situated wholly in British India in that year, or (b) if its income arising in British India in that year exceeds its income arising without British India in that year. It is not suggested that paragraph (a) is invalid. The provision that the residence of a company depends on where the control and management of its affairs is situated is in accordance with English law. But it is suggested that paragraph (b) is *ultra vires* in that it involves the taxation of a non-resident in respect of income derived outside British India.

The facts found by the Tribunal are that the assessee, Wallace Bros. & Co., Ltd., is a company incorporated in the United Kingdom, that the control and management of its affairs is situated wholly in that country, and that the company has no director in India, but is a sleeping partner in the firm of Messrs. Wallace & Co., which carries on, and has a place of, business in Bombay. What exactly is meant by the expression "sleeping partner," I am not sure. Seeing that the English company is entitled under the articles of partnership to a 14/82 share in the profits of the Bombay firm and that it can dismiss any other partner on six months' notice, I apprehend that, although it may leave the management of the affairs of the firm in India to the partners resident in India, its views on matters of general policy are likely to meet with considerable respect from those partners. However, I do not think it matters what the exact relationship of the partners *inter se* may be; it is sufficient to find that the assessee-company is a partner in the firm of Wallace & Co., which carries on business in Bombay. The share of the assessee-company in the profits of Wallace & Co., for the accounting year was something over eight lacs, and it had other income derived from British India, bringing the total to over seventeen lacs, and its income accruing or arising outside British India in the material year was about seven and a half lacs. I should have said that the year of assessment is the year 1939-40, so that the accounting year is 1938-39, and these figures relate to the accounting year. It is therefore clear that in respect of the accounting year the income of the assessee-company arising in British India exceeded its income arising without British India.

In order to understand the effect of Section 4-A of the Indian Income-tax Act, it is necessary to look at some of the other provisions. Section 3 is the charging section, which provides that where any Act of

the Central Legislature enacts that income-tax shall be charged for any year at any rate or rates tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of, the Act in respect of the total income of the previous year. Then Section 4 (1) provides, so far as material, that the total income of any previous year of any person includes all income, profits and gains from whatever source derived which (a) are received or are deemed to be received in British India in such year by or on behalf of such person, or (b) "if such person is resident in British India during such year, (i) accrue or arise to him in British India during such year, or (ii) accrue or arise to him without British India during such year," or (c) "if such person is not resident in British India during such year, accrue or arise or are deemed to accrue or arise to him in British India during such year." So that a person resident in British India has to pay tax on income which accrues or arises to him without British India during the year in addition to the income accruing or arising within British India. Then Section 4-A defines what is meant by "residence in British India." It says:

"For the purposes of this Act—(a) any individual is resident in British India in any year if he—(i) is in British India in that year for a period amounting in all to one hundred and eighty-two days or more."

Then there are other circumstances enumerated which constitute residence of an individual. Then comes sub-section (c) which is the material one, and which I have already read, and so far as relevant for the present purpose it provides that a company is resident in British India if any if its income arising in British India in that year exceeds its income arising without British India in that year. That sub-section plainly justifies the present assessment, if it is valid, but the contention of the assessee is that it is *ultra vires*.

Now, the Indian Legislature is not, as we know, a Sovereign Legislature. Its powers are conferred by the Government of India Act, 1935, but within the ambit of the very wide legislative powers conferred by that Act the Indian Legislature is a Sovereign Legislature. The question whether or not this sub-section is *ultra vires* must necessarily turn on the construction of the Government of India Act, the contention of the assessee being that it is incompetent for the Government of India to provide that the income of a non-resident which accrued outside British India shall be subjected to Indian income-tax, because that would be extra-territorial legislation of a character not sanctioned by the Act.

Before I discuss the terms of the Government of India Act, I will notice one or two arguments advanced by Sir Jamshedji Kanga,

arguments of a more or less general character designed, I think, to induce in us a state of mind sympathetic towards the construction he desires us to adopt when we approach the Act. He points out, in the first place, that the English system of income-tax taxation is to tax a resident in England upon the whole of his income derived from any source and from any place, and to tax income derived from any property in England wherever the owner of the property may be resident, and from that English practice he affirms a fundamental principle underlying all income-tax legislation that you can only tax a person resident, or property situate, within the taxing country. But the English Legislature is a Sovereign Legislature, and there is nothing whatever to prevent it from extending its practice by imposing income-tax on foreign income of a non-resident in cases where there are assets within the country which enable such taxation to be effective. It is, in my opinion, impossible to maintain that, because the English Legislature has not chosen to tax income of that nature, therefore no other system of legislation can tax such income. Nor am I impressed with the argument, which found some favour with the learned Chief Justice of Calcutta in a case to which I will refer presently, that one ought in construing the Government of India Act to approach the matter with a presumption that the English Parliament did not intend to confer upon the Indian Legislature a power which it possessed itself, but had never thought it desirable to exercise. Conditions in England and India are quite dissimilar. There is no evidence on the point, but it may well be, and I have no doubt in my mind that it is a fact, that in British India a much larger proportion of businesses send a part of their profits out of the country than is the case in England, and I see no reason, therefore, why the Indian Legislature should not be empowered to impose taxation on a class of income which the English Legislature has left alone. It was said that this English practice constituted a sort of legislative practice, which tended to show that it cannot have been intended that income of this sort should be subjected to taxation. I do not think in this case any question of legislative practice arises, because we are not called upon to consider the construction of any particular words of the Government of India Act, so that we cannot be asked to construe them in the light of former legislative practice.

Then it was argued that the only moral justification for imposing income-tax, if one may use such an expression in relation to such a subject, was that a man is taxed in return for the protection afforded him by the laws of the taxing country. But that argument does not help here, because it is the basis of sub-section (c) of Section 4-A (which I will refer to as "the impugned sub-section" that the bulk of the

assessee's income is derived from British India, and, therefore, is earned under the protection of British Indian laws.

Then it was argued by Sir Jamshedji that there was something unfair and improper in taxing the foreign income of a non-resident. In opening he did not go so far as to say that such a provision would be contrary to natural justice, but he could not resist saying so in reply. But, with all respect, there does not seem to me anything inherently unfair in providing that a man who earns income in British India, but does not reside here, should be taxed rather more heavily than a man who does reside here, and who, therefore, spends his income in this country, and engages in those social services which a normal resident, in greater or less degree according to his taste, does engage in. However, all these arguments, as I have said, were only designed to induce us to approach the construction of the Government of India Act in a spirit sympathetic to the assessee's case.

Now, coming to the Government of India Act, Section 99 (1), read with Section 316, provides that, subject to the provisions of the Act, the Indian Legislature may make laws for the whole or any part of British India, and a Provincial Legislature may make laws for the Province. In that sub-section there is no reference whatever to extra-territorial legislation, though the object of legislation must be British India. But sub-section (2) provides that without prejudice to the generality of the powers conferred by the preceding sub-section, no Indian law shall, on the ground that it would have extra-territorial operation, be deemed to be invalid in so far as it applies to five matters of legislation which are therein enumerated. That sub-section seems to show that the Legislature realised that the general power in Section 99 (1) to make laws for the whole or any part of British India might involve a question as to whether a law with extra-territorial effect would come within the power. The Legislature thought of five matters, on which a doubt might arise, and expressly dealt with them; but it realised that there might be others and, hence the opening words of sub-section (2), "Without prejudice to the generality of the powers conferred by the preceding sub-section." Then Section 100 and the Seventh Schedule enumerate in three lists the matters on which the Indian Legislatures may make laws, the first list being matters on which the Central Legislature can legislate, the second list being those on which the Provincial Legislature may legislate, and the third list being matters on which the Central and the Provincial Legislatures may both legislate. It is to be noticed in passing that several of the items in the first list involve some sort of extra-territorial operation, for instance, items 22 to 25. Item 54 in List I deals with income-tax, and includes "Taxes

on income other than agricultural income." Taxes on agricultural income are included in the Provincial list. So that two things seem to me clear from those sections and the Seventh Schedule, first, that the mere fact that an Act of the Central Legislature has some extra-territorial operation is not enough to invalidate it, and, secondly, that the power to impose income-tax is vested in the Indian Legislature.

Sir Jamshedji Kanga contends that the impugned sub-section is of purely extra-territorial effect. That is clearly going too far, since the basis of the sub-section is that the bulk of income has been earned in British India. On the other hand, Mr. Setalvad, for the Commissioner of Income-tax, maintains that, properly considered, the sub-section has no extra-territorial effect, and he has referred us to certain authorities of the Federal Court of Australia in which the meaning of the expression "extra-territorial legislation" has been considered. I do not think it necessary to go into that question in any detail, because there is no expression in the Government of India Act which we are called upon to interpret which mentions extra-territorial legislation. There is clearly no provision in the Act which says that any extra-territorial legislation shall be outside the powers of the Indian Legislature. I will only refer to one passage in *Colonial Gas Association Ltd. v. Federal Commissioner of Taxation*¹ from the judgment of Mr. Justice Dixon, in which he says :

"To derive income from a country involves the person deriving it in a territorial connection with the country sufficient to support the validity of an exercise of the power in respect of the person as distinguished from the income."

That is to say, if a person is deriving income from a business carried on in a country, he has a sufficient territorial connection with that country to prevent a law imposing tax upon him being regarded as extra-territorial. Mr. Setalvad contends that inasmuch as the whole basis of the liability to tax under the impugned sub-section is based on the bulk of the assessee's income arising in British India, the sub-section would not fall within an express prohibition against any extra-territorial legislation. It is, no doubt, true that there is some extra-territorial effect in the impugned sub-section. It does enable the foreign income of a non-resident to be taxed. But other sections have some extra-territorial effect, for instance Section 4-A (a) (i), which directs that an individual shall be regarded as resident in British India if he has been there for a period amounting to one hundred and eighty-two days ; so that, although he has been in India only for half a year, he is to be taxed for the whole year ; in that sense there is some

(1) (1934) 51 Commonwealth L.R. 172, at p. 187,

extra-territorial effect in that provision. So I think there is in Section 42, which enables a non-resident to be taxed in respect of income derived from a business connection in British India. That extra-territorial effect is not so great as in the case of the impugned sub-section, because the income taxed under Section 42 must be derived from British India; but still it does enable a non-resident to be taxed. If one is going to say that the Government of India Act precludes all legislation which has any extra-territorial effect, it would be difficult to justify, not only the impugned sub-section, but Section 4-A (a) (i) and Section 42. But, as I have said, there is nothing in the Government of India Act which lays it down that any legislation having any extra-territorial effect is invalid, and short of such a prohibition, I cannot see any principle on which the impugned sub-section can be held to be *ultra vires*. Whether it is impolitic as being calculated to drive capital out of the country, it is not for us to consider. As the Tribunal has pointed out, in the ultimate analysis the effect of the sub-section is to increase the amount of the assessment on the taxpayer. In clothing a company with an artificial residence for the purpose of income-tax, the Income-tax Act is merely employing machinery for levying additional tax in relation to income arising within British India. The same result could be achieved by providing that in the case of an assessee who is shown to possess income arising outside British India the amount of his assessment should be increased proportionately to the amount of his income accruing outside British India.

Referring to some of the cases cited, there is, I think, no doubt from the English cases in the House of Lords, particularly *Egyptian Delta Land and Investment Co. v. Todd*¹ and *Swedish Central Railway Co. v. Thompson*², that, in the case of a company, residence is always artificial, and should be the subject of express legislative enactment, and furthermore that a company may have two places of residence. There can, therefore, be no objection to the impugned sub-section merely because it enacts a definition of an artificial character in respect of the residence of companies. It seems to me clear from the power of the Central Legislature to impose income-tax that that Legislature must have power to determine who is to pay the tax, and for that purpose to lay down rules as to who is to be regarded as resident in, and what income is to be deemed to arise in, British India. I can see no real basis for the assessee's argument.

We were referred to a very recent decision of the Calcutta High Court in *Raleigh Investment Co., Ltd. v. Governor-General in Council*³ in which the Court held that Explanation (3) to Section 4

(1) (1929) A.C. 1.

(2) (1925) A.C. 495.

(3) Sait No. 533 of 1942, since reported in (1943) 11 I.T.R. 393.

of the Indian Income-tax Act was *ultra vires*, no doubt partly on the ground that it was of an extra-territorial character. I do not find myself in agreement with all the views expressed by the learned Judges in that case, but the actual decision has no operation on the matter before us. There may be much more to be said for the invalidity of Explanation (3) than for the invalidity of the sub-section with which we have to deal.

In my opinion, the contention that Section 4 A (c) is invalid is not well founded, and that really disposes in substance of all the questions.

The first question is :

“Whether in the circumstances found by the Tribunal in its order under Section 33 the assessee-company was taxable to income-tax and super-tax for the assessment year 1939-40 in respect of the income (Rs. 7,48,437 less Rs. 4,500) which accrued or arose to it without British India in the previous year?”

The answer is in the affirmative.

The second question is :

“Are the provisions of Sections 4-A (c) and 4 (I) (b) (ii) of the Income-tax Act *ultra vires* the Indian Legislature?”

The answer is in the negative. The answer to this question depends on that to the first one.

The third question is :

“Is sub-clause (b) of Clause (c) of Section 4-A of the Amended Act applicable to the assessment of the assessee-company for the year 1939-40?”

I gather that the argument before the Tribunal was that retrospective effect could not be given to the impugned sub-section, but, as the Tribunal points out, there is no question of giving retrospective effect. No doubt, the Amended Act came into operation after the close of the previous year, but under that Act income of the previous year has to be ascertained in accordance with the provisions of the Amended Act in order to determine the assessment for the current year. Sir Jamshedji Kanga raised a further point that the sub-section did not apply, because there was no finding that the assessee was to be treated as resident in British India in the year of assessment, the finding only relating to the previous year. But, in my opinion, it is only the previous year which is relevant. So that the third question must be answered in the affirmative.

The fourth question is :

“Whether on the facts found by the Tribunal the Additional Income-tax Officer, Companies Circle, Bombay, had jurisdiction under Section 64 (1) or Section 64 (2) to make the assessment?”

Under Section 64 (1) the assessment has to be made by the Income-tax-Officer of the area in which the assessee's place of business is situate. Here the assessee has been found to be a partner in the firm of Wallace & Co., and the assessment was made by the Income-tax Officer for the areas in which Wallace & Co., carry on business. Therefore, it seems to me plain that the answer to question 4 is that the Officer had jurisdiction under Section 64 (1). The question whether jurisdiction also arose under Section 64 (2) does not arise.

Sir Jamshedji Kanga was anxious to raise certain other questions, which the Tribunal had been asked, and had refused to raise, but we can only deal with questions before us. As far as we can judge, they adequately raise all the questions which can properly be raised, and we see no reason whatever for amending or adding to such questions.

The assessee must pay the Commissioner's costs.

RAJADHYAKSHA, J.—I agree and have nothing to add.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME-TAX, BOMBAY

v.

BOMBAY BARODA AND CENTRAL INDIA RAILWAY CO.

SIR JOHN BEAUMONT, C. J., AND RAJADHYAKSHA, J.

July 23, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 4-A (c), 10 (2) (iii)—INCOME—RAILWAY COMPANY—RESIDENCE—CONTROL AND MANAGEMENT SITUATED OUTSIDE BRITISH INDIA—INTEREST ON DEBENTURES PAID BY SECRETARY OF STATE IN ENGLAND OUT OF REVENUES OF INDIA—WHETHER INCOME OF COMPANY—WHETHER INCOME ARISING IN BRITISH INDIA EXCEEDS INCOME ARISING OUTSIDE BRITISH INDIA—STATUS OF COMPANY—GUARANTEED INTEREST PAID ON CAPITAL—WHETHER DEDUCTIBLE UNDER SEC. 10 (2) (iii).

The assessee was the Bombay Baroda and Central India Railway Company whose control and management was situated outside British India. The material portion of a contract between the assessee and the Secretary of State of India provided as follows: "The Secretary of State will, as often as and when the half-yearly or other interest payable in respect of any debentures or debenture stock that may be sanctioned and issued as aforesaid, or in respect of any portion of such debentures or debenture stock, shall become due, pay in London in

sterling out of the revenues of India to the Company the aggregate amount of such interest as a fund to meet and provide for the payment of such interest to the persons entitled thereto." The assessee claimed that it was not resident in British India under Section 4-A (c) of the Income-tax Act, inasmuch as its income arising in British India was less than its income arising outside British India. That depended on whether the amount of Rs. 4,66,667 representing the interest on debenture stock paid by the Secretary of State in England under the terms of the contract was income of the Company arising without British India within the meaning of Section 4-A (c) of the Act.

Held, that the amount of Rs. 4,66,667 was paid to the Company earmarked for a particular purpose, namely the payment of interest on debentures, and it never formed part of the income of the Company. Consequently the Company was resident in British India within the meaning of Section 4-A (c) of the Act;

Held further, that the payments made in respect of the guaranteed interest of Rs. 8,00,000 were not deductible from the income of the company under Section 10 (2) (iii) of the Act.

Case stated under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay, Sind and Baluchistan : (Income-tax Reference No. 11 of 1943).

STATEMENT OF CASE

" My Lords,

Under Section 66 (2) of the Indian Income-tax Act, XI of 1922, (hereinafter referred to as "the Act") and at the instance of the Bombay Baroda and Central India Railway Co. (hereinafter referred to as "the Company") I have the honour to refer for your Lordships' decision the questions of law stated in paragraph 12 below which arise from the assessment of the Company for the year 1939-40, the relevant accounting period being the year ending on the 31st of March 1939.

2. **Facts of the Case.**—The Company was reconstituted by an Act of Parliament in 1906. The Act was passed in consequence of the purchase by the Secretary of State for India in Council of the property vested in the former Bombay Baroda and Central India Railway Co. A provisional contract containing the terms on which the railway was to be worked and managed by the new Company as from the 1st of January 1906 on behalf of the Secretary of State was signed on the 27th of December 1905, pending the execution of a new contract which is known as the "principal contract" and which was signed on the 8th of April 1907. Two other contracts dated the 15th of October 1908 and

the 24th of October 1913 deal with the issue of debentures and with modifications in the principal and debenture contracts.

3. The Act of 1906 fixed the purchase price at £ 11,685,581, and the Secretary of State agreed to create and issue to the Company India 3 per cent. stock to the nominal value of £ 10,089,146 in satisfaction of £ 9,685,581 of the purchase price. For the remainder of the purchase price the Company was to raise a new capital of £ 2,000,000 on which the Secretary of State guaranteed interest at the rate of 3 per cent. A similar rate of interest was guaranteed on any further ordinary stock which the Company might issue with the approval of the Secretary of State during the continuance of the principal contract. Under the terms of the contract dated the 15th of October 1908 interest was also guaranteed on any debentures or debenture stock which might be issued by the Company with his approval.

4. The provisions relating to the guarantee of interest on the capital of the Company are stated in clause 7 of the principal contract. That clause, as amended by the contract dated the 24th of October 1913, reads as follows :—

“During the continuance of this contract the Secretary of State shall, out of the revenues of India, pay to the Company in London half-yearly, on the 1st day of January and the 1st day of July, interest at the rate of three per cent. per annum calculated to the 31st day of December and the 30th day of June respectively on the said capital of £ 2,000,000, such interest to be deemed to have commenced from the 31st day of December 1905, the first payment thereof having been made to the Company on the 2nd day of July 1906.

The Secretary of State shall in like manner pay to the Company on the same half-yearly days interest at the rate of 3 per cent. per annum calculated to the 31st day of December and the 30th June respectively on the amount which shall for the time being have been paid to his credit in respect of any further ordinary stock which the Company may during the continuance of the Principal Contract issue with his sanction (excluding any sum paid by way of premiums on such stock). Such interest shall commence from the date on which the said amount shall have been paid to the credit of the Secretary of State. Any interest paid by the Secretary of State under this clause shall be treated as a fund to meet and provide for the payment to the holders of the Company's said capital stock of £ 2,000,000 and any further ordinary stock which the Company may, during the continuance of the Principal Contract, issue with the sanction of the Secretary of State, of the guaranteed interest at the rate of 3 per cent. per annum payable in

respect thereof, and shall be applied to such payment accordingly and to no other purpose."

5. The corresponding provisions with regard to the guarantee of interest on debentures are contained in clause 2 of the contract dated the 15th of October 1908 which reads as follows :—

"The Secretary of State will, as often as and when the half-yearly or other interest payable in respect of any debentures or debenture stock that may be sanctioned and issued as aforesaid, or in respect of any portion of such debentures or debenture stock, shall become due, pay in London in sterling out of the revenues of India to the Company the aggregate amount of such interest as a fund to meet and provide for the payment of such interest to the persons entitled thereto, and will, on the respective days on which the principal moneys represented by such debentures or debenture stock shall, according to the terms of the debentures or in the case of debenture stock, of the terms of issue thereof, be payable, and so as duly to provide for the payment of such principal moneys to the persons entitled thereto when respectively due, pay in London in sterling to the Company the amount of the principal sums payable on such respective days; and the moneys so to be paid to the Company under this clause shall be paid to and received by it for the respective holders for the time being of the said debentures or debenture stock, and placed by the Company in the Union of London and Smith's Bank or some other bank to be agreed upon, to an account to be called "The Bombay Baroda and Central India Railway Company's Debenture Capital Account," and shall be applied to the respective payments of such interest and principal accordingly, and to no other purpose. The moneys payable under this clause to the Company as aforesaid shall be paid without regard to any set-off, lien, charge, claim, or equity which the Secretary of State may have against the Company. Provided always that in every case in which the holder of any debentures or debenture stock shall not, within a period of twelve calendar months after the principal moneys payable in respect of such debentures or debenture stock shall have become payable, have applied for the payment of such moneys, then such moneys shall be carried to the account of the Secretary of State, and in every case in which any interest payable in respect of any of the said debentures or debenture stock shall be unclaimed for a period of two years after the same shall have become due, such interest shall also be carried to the account of the Secretary of State. And the Secretary of State hereby undertakes to indemnify and hold harmless the Company against all claims in respect of principal or interest which shall have been so carried to the account of the Secretary of State as being unclaimed

within such respective periods as aforesaid, and generally against all liability incurred or to be incurred by the Company by reason of their acting on the foregoing proviso."

6. Clauses 50 and 51 of the principal contract, as amended by the contract dated the 24th of October 1913, contain the following provisions with regard to the distribution of the profits of the undertaking between the Company and the Secretary of State :—

" 50 (a). From the gross receipts of the undertaking in each half year shall be deducted the working expenses of the undertaking, and all other charges to Revenue account properly attributable to such half-year ; and the remainder together with the interest to be credited by the Secretary of State under clause 19 of the Supplemental Contract of the 24th October 1913, shall be the net receipts of the undertaking for such half year.

(b) From such net receipts shall be deducted the total of the following sums :—

(1) The amount by which the gross earning for such half-year of the subsidiary lines forming part of the undertaking shall exceed the sums payable to the Company in respect of the working of such subsidiary lines.

(2) Allowances for rebate and direction and other deductions referred to in Section 46.

(c) The residue of the net receipts of the undertaking for each half year after the deduction mentioned in sub-clause (b) shall be applied in the following manner and in the following order :—

(i) In repayment to the Secretary of State in rupee currency (calculated at the prescribed rate of exchange) of the interest payable by the Secretary of State for such half year on any debentures or debenture stock of the Company which shall have been created and issued with the sanction of the Secretary of State after the 31st December 1905.

(ii) In the next place, in payment to the Secretary of State and the Company *pari passu* of interest at the rate of 4 per cent. per annum on the average amount during the half year of the preferred capital of the Secretary of State and the average amount during the same period to the credit of the Company's capital account respectively, such average amounts to be calculated in the manner prescribed in paragraph (iv) of this sub-clause.

(iii) If such residue as aforesaid of the net receipts attributable to either half year in any year, and applicable in the manner mentioned in the preceding paragraphs of this sub-clause, shall exceed the amount of payments chargeable thereon under the same paragraphs,

the surplus arising from such excess of such residue of net receipts over the payments to be made thereout shall be applied, so far as such surplus shall extend, in making good the deficiency (if any) of such residue as aforesaid of the net receipts attributable to the other half of such year as compared to the payments chargeable on such residue of net receipts under the preceding paragraphs of this sub-clause.

(iv) If the aggregate of such residue as aforesaid of the net receipts attributable to the two half years of any year shall exceed the aggregate amount of the payments chargeable thereon under paragraphs (i), (ii), and (iii) of this sub-clause, the surplus thus arising shall be first applied in payment of interest for the year at the rate of 4 per cent. on the amount for the time being of the deferred capital of the Secretary of State, and the balance if any thereafter remaining shall be divided between the Secretary of State and the Company in proportion to the average amounts during the year as calculated month by month standing to the credit of the Secretary of State and the Company respectively in the Government capital account and the company's capital account respectively, including in the capital of the Secretary of State both his preferred and his deferred capital. In the calculation of the average amount for any month of the capital of the Secretary of State and the Company respectively the average amount for any month shall be taken to be one half of the sum of the respective amounts of such capital on the first day and the last day of the month respectively.

(v) Any moneys which the Company shall be entitled to receive under this sub-clause shall be receivable by the Company in India and not elsewhere.

51. The amount of the interest payable by the Secretary of State to the Company in respect of any half year under Clause 7 of the Principal Contract as hereby varied shall be deducted from the interest at the rate of 4 per cent. per annum payable to the Company in respect of the same half year under the last preceding clause and shall be retained by the Secretary of State."

7. The manner in which these provisions were carried out is shown by statement No. XIII (c) in the Capital and Revenue Accounts of the Company for the year ending on the 31st of March 1939. A copy of this statement is annexed as exhibit A. From the total receipts of the year are first deducted all expenses incurred in the course of the business and certain charges which include the guaranteed interest on the debenture stock. Provision is then made for the interest on the Company's capital at the rate of 4 per cent. prescribed by clause 50 of the principal contract and for interest on the Government capital.

The balance constitutes the "surplus profits" which are divided in accordance with the agreement. To the Company's share of the surplus profits is added the amount of interest payable on its capital and from the total sum so computed the Secretary of State recovers, under clause 51 of the principal contract, the guaranteed interest of 3 per cent. which is paid to the Company in England each half year.

8. In the assessment year 1939-40 the question whether the Company was resident or not resident in British India assumed a new importance in view of the changes introduced by the Income-tax (Amendment) Act, 1939, which came into force on the 1st of April 1939. Under Section 4-A (c) of the amended Act "a company is resident in British India in any year (a) if the control and management of its affairs is situated wholly in British India in that year, or (b) if its income arising in British India in that year exceeds its income arising without British India in that year." In the present case the control and management of the Company is admittedly situated outside British India, but the question whether its income arising in British India exceeds its income arising without British India is disputed.

9. In its return for the relevant accounting period the Company declared an income of Rs. 11,04,225 arising in British India and an income of Rs. 13,75,595 arising outside British India, and it therefore claimed to be "non-resident." The Income-tax Officer accepted the declaration with regard to the British Indian income, but he found that the Company had included in its income arising outside British India the sum of Rs. 4,66,667 which had been paid by the Secretary of State in respect of debenture interest. He held that this was not income of the Company for the purposes of Section 4-A of the Act and he proceeded to compute the income arising outside British India as follows:—

| | Rs. |
|--------------------------------------------------------------|----------|
| 3 per cent. guaranteed interest on capital of £20,00,000 ... | 8,00,000 |
| Interest on deposits, investments, etc. ... | 1,08,965 |
| Total ... | 9,08,965 |

Since this was less than the British Indian income he treated the Company as "resident" and made an assessment on a total income of Rs. 20,08,690 after allowing the deduction of Rs. 4,500 which was admissible under the third proviso to Section 4 (1) (c) of the Act. A copy of the assessment order is annexed and marked B.

10. The Company then appealed to the Appellate Assistant Commissioner, B-Range, Bombay. In the grounds of appeal the Company repeated the contention raised before the Income-tax Officer with regard to the debenture interest and further prayed that in case it was held to

be resident in British India the sum of Rs. 8 lakhs, being the 3 per cent. guaranteed interest on the Company's capital, should be excluded from the assessment on the ground that the whole amount represented interest on capital borrowed for the purposes of the business, which is allowable as a deduction under Section 10 (2) (iii) of the Act. The Appellate Assistant Commissioner rejected both of these claims but he accepted the Company's contention with regard to a minor point and allowed a reduction of Rs. 3,802 in the income arising outside British India. A copy of the appellate order is annexed and marked C.

11. Thereafter the Company submitted an application to the Commissioner of Income-tax, Bombay, under Sections 38 and 66 (2) of the Act in which it requested the Commissioner either to revise the assessment or to make a reference to the High Court. A copy of the application is annexed and marked D. As I am not prepared to exercise my powers of revision, I have agreed to make a reference on the questions of law which arise from the appellate order.

12. *Questions for Decision.*—I accordingly refer the following three questions for your Lordships' decision :—

(1) Whether the amount of Rs. 4,66,667 representing the $3\frac{1}{2}$ per cent. interest on debenture stock paid by the Secretary of State in England is "income" of the Company arising without British India within the meaning of Section 4-A (c) of the Act.

(2) Whether in the circumstances of the case the Company has been rightly held to be "resident" in British India within the meaning of Section 4-A (c) of the Act.

(3) Whether the payments made in respect of the guaranteed interest of Rs. 8,00,000 are deductible from the income of the Company under Section 10 (2) (iii) of the Act.

13. *Opinion of the Commissioner.*—The Act prescribes certain deductions which are to be allowed in the computation of the income of an assessee, and in the absence of any indication to the contrary the word "income" in Section 4-A (c) of the Act should, in my opinion, be interpreted as referring to the income computed in accordance with these provisions. I submit therefore that the income which has to be considered for the purpose of Section 4-A (c) is the net income of the Company, after the allowance of the prescribed deductions, and not the gross receipts. Under clause 2 of the contract, dated the 15th of October 1908, which has been quoted in paragraph 5 above, the amount paid by the Secretary of State in respect of the debenture interest is received by the Company on behalf of the holders of debenture stock and has to be placed in a special account and used only for the payment of the amounts due to them. The interest payable to debenture holders is

admissible as a deduction under Section 10 (2) (iii) of the Act, and since the whole of the amount received from the Secretary of State is in fact paid out there remains no income from this source which can be taken into consideration in the assessment of the Company. I submit therefore that the amount received in respect of the debenture interest is not "income" for the purposes of the Act.

Even if the amount in question could be regarded as 'income' it would not in my opinion be income arising without British India. Although the interest is actually paid in London, clause 2 of the contract dated the 15th of October 1908 clearly states that it is payable "out of the revenues of India," and it is treated in the accounts (exhibit A) as a charge on the profits earned by the Railway in India. I submit that such income should be regarded as income arising in British India. In this connection I venture to invite a reference to the decision of the Madras High Court in the case of the *Madras & Southern Mahratta Rly. Co.*¹

14. The answer to the second question depends upon the answer given to the first. If the amount paid in respect of debenture interest is held not to be income for the purposes of the Act, or to be income arising in British India, the total amount of income arising in British India will clearly be greater than the total amount of income arising elsewhere and the Company will therefore be "resident" in British India for the purpose of Section 4-A (c) of the Act.

Although it did not affect the question of the Company's residence in the present case I would further submit that the Income-tax Officer and the Appellate Assistant Commissioner have in fact erred in treating the sum of Rs. 8 lakhs which was paid in respect of the guaranteed interest on the ordinary stock of the Company as income arising without British India. In so doing they were doubtless following the decision of the Calcutta High Court in the case of the *Bengal Nagpur Railway Co.*², but in *Commissioner of Income-tax, Madras v. The Madras & Southern Mahratta Railway Co.*¹, the Madras High Court have dissented from the view taken in the Calcutta case. It has been argued that the present case is distinguishable from that of the *Madras and Southern Mahratta Railway Co.*, since the Madras Company is not allowed to use any of the receipts of the undertaking for the purpose of meeting working expenses and the distribution of the profits rests entirely with the Secretary of State who is entitled, in calculating the surplus, to deduct the equivalent in rupees of the amount which he has paid to the railway company by way of guaranteed interest in the course of the year, whereas in the present case the full amount of the interest on the

(1) (1940) 8 I.T.R. 280.

(2) (1922) 1 I.T.C. 178.

Company's capital is deducted from the earnings of the railway before one arrives at the surplus profits which are to be divided between the Company and the Secretary of State. I submit however that this difference does not materially affect the question now under consideration. In the Madras case it was held that the amounts paid to the shareholders were income arising in British India because they were in fact paid out of the proceeds of the working of the railway. In the present case the whole of the profits of the undertaking are earned in India and the payment made by the Secretary of State in London is merely an advance payment which is subsequently adjusted against the Company's share of the Indian profits. The payment in question should therefore, in my opinion, be regarded as income arising in British India.

It may be added that the question whether the payment in London of the guaranteed interest would constitute income arising in British India if the profits of the undertaking were insufficient to cover that interest was left open in the *Madras and Southern Mahratta Company's case*¹. Although this contingency has not arisen in the present case I venture to point out that under Section 42 (1) of the Act, as amended by the Income-tax (Amendment) Act, 1939, income arising "through or from any asset or source of income in British India or through or from any money lent at interest and brought into British India in cash or in kind" is deemed to be income accruing or arising in British India. Thus even if the Company were not resident the income of Rs. 8 lakhs from the guaranteed interest would be chargeable as income deemed to accrue or arise in British India and the company would not be in a position to claim that it was not liable to be taxed in British India in respect of that income.

15. As regards the third question I submit that the payments made to the ordinary shareholders out of the guaranteed interest paid by the Secretary of State are clearly distinguishable from the interest paid to the debenture holders and cannot be said to be interest paid in respect of capital borrowed for the purposes of the business. These payments are interest paid on the share capital of the Company and as such they are not covered by Section 10 (2) (iii) of the Act. They represent an appropriation of profits and not an expenditure incurred for the purpose of earning the profits. I submit therefore that the deduction claimed by the Company is not admissible under the provisions of the Act.

16. For the above reasons I am respectfully of opinion that questions (1) and (3) should be answered in the negative and question (2) in the affirmative."

(1) (1940) 8 I.T.R. 280.

V. F. Taraporewalla with C. K. Daphtary, for the Assessee.
M. C. Setalvad with G. N. Joshi, for the Commissioner.

JUDGMENT.

BEAUMONT, C. J.—This is a reference made by the Income-tax Commissioner under Section 66 of the Indian Income-tax Act. The year of assessment is the year 1939-40, but an application was made to the Commissioner to make a reference in July 1940, the Assistant Commissioner's order in appeal having been made on the 31st of May in that year. For some reason or other the reference was not made until the 1st of June 1943. On the 25th January 1941 Part II of the Amended Income-tax Act had come into operation, and, therefore, an appeal would lie to the Appellate Tribunal, and it would be for them to make a reference. But Section 14 of Act XL of 1940 reserves power to the Commissioner to make a reference in cases already pending before him when Part II came into operation. So I think the Commissioner was entitled to make the reference.

The questions appear at first sight to be a good deal more formidable than they are shown to be when one understands the position, because the contracts, and the financial arrangements existing between the assessee, Bombay Baroda and Central India Railway Company, and the Secretary of State for India are of a complicated character but the questions raised are really simple.

The first question is: "Whether the amount of Rs. 4,66,667 representing the $3\frac{1}{2}$ per cent. interest on debenture stock paid by the Secretary of State in England is 'income' of the Company arising without British India within the meaning of Section 4-A (c) of the Act." Section 4-A defines "residence in British India," and sub-section (c) enacts that "a company is resident in British India in any year (a) if the control and management of its affairs is situated wholly in British India in that year,"—admittedly in this case the control was not in British India—"or (b) if its income arising in British India in that year exceeds its income arising without British India in that year." The claim of the company is that its income arising in British India is less than the income arising outside British India, and that depends on whether this sum of Rs. 4 lacs odd of interest on debenture stock can be regarded as income of the company arising out of British India. It is paid in London, although out of the revenues of India. I should think that if it can be fairly described as income of the Company, it may be said to arise out of British India. But when one looks at the contract under which the liability of the Secretary of State to pay interest on debentures arises, it seems to me quite clear that these

payments of interest on debentures never formed part of the income of the Company. The contract provides that "The Secretary of State will, as often as and when the half-yearly or other interest payable in respect of any debentures or debenture stock that may be sanctioned and issued as aforesaid, or in respect of any portion of such debentures or debenture stock, shall become due, pay in London in sterling out of the revenues of India to the Company the aggregate amount of such interest as a fund to meet and provide for the payment of such interest to the persons entitled thereto." So that, it is paid as a fund to meet a particular debt of the Company, that is to say, interest on debentures, and admittedly the Company keeps the money on a separate account. Therefore, in my opinion, it never forms part of the income of the Company. If the contract had been to pay so much a year to the Company, the amount being based on the amount which would have to be paid to the debenture-holders by way of interest, but the money forming part of the general revenue of the Company, then it might be said to be income of the Company, and in that case presumably the Company would have to pay income-tax upon it in England. But as the contract is worded, it seems to me that it never formed part of the income of the Company. Analogous questions frequently arise in insolvency and if the assessee were an individual, and became insolvent, I think undoubtedly the debenture-holders could claim this fund as fund earmarked to pay their interest, and would not be required merely to prove with other creditors. The test is whether the money is paid to the Company earmarked for a particular purpose, or as part of its general revenue, and I have no doubt that it is paid earmarked for a particular purpose. Therefore, the answer to the first question is in the negative.

The second question is: "Whether in the circumstances of the case the Company has been rightly held to be 'resident' in British India within the meaning of Section 4-A (c) of the Act." The answer to that question will be in the affirmative. It follows on the answer to the first question.

I may observe that the assessee asked leave to raise a question whether Section 4-A (c) of the Income-tax Act is *ultra vires*. That question was raised in the last reference¹ which we heard, and we held that the section is *intra vires* the Indian Legislature. As the assessee did not ask the Commissioner within the prescribed time to raise that point, I think the Commissioner rightly refused to raise it.

Then the third question is this: "Whether the payments made in respect of the guaranteed interest of Rs. 8,00,000 are deductible from

(1) *Wallace Bros. & Co., Ltd. v Commissioner of Income-tax, Bombay* (1943) 11 I.T.R. 559,

the income of the Company under Section 10 (2) (iii) of the Act." The only point in that question really arises from the inaccurate use of the word "interest," because when one ascertains the facts, the so-called interest is really dividend on shares. In effect the Secretary of State has guaranteed a dividend of 3 per cent. on certain shares. As we all know, dividends are payable out of profits, and if the profits of the Company are sufficient and a dividend is declared of over 3 per cent., then the Secretary of State's obligation does not arise. But if the Company does not declare a dividend of 3 per cent. on the shares, then the Secretary of State has to make up the amount. But the sum is a sum paid in order to make up profits to the amount necessary to enable the dividend to be paid. In no sense it is a deductible liability under Section 10 (2) of the Act. It makes no difference that in practice the Secretary of State pays the amount to the Company before it is determined whether to pay a dividend, and if so at what rate, and subsequently recovers the amount if his obligation to pay does not in the events arise. The third question must be answered in the negative.

The assessee to pay costs.

RAJADHYAKSHA, J.—I agree.

Reference answered in the affirmative.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS

v.

M. AHMAD BADSHA SAHEB.

SIR LIONEL LEACH, C. J., and LAKSHMANA RAO, J.

October 15, 1948.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 4 (3) (vii)—CASUAL AND NON-RECURRING RECEIPT—MERCHANT ACTING AS ARBITRATOR IN A DISPUTE AMONG HEIRS—NO STIPULATION FOR REMUNERATION—AMOUNT PAID AS REWARD FOR SERVICES—WHETHER ASSESSABLE.

The assessee, a merchant, agreed to act as an arbitrator in a dispute which arose among the heirs of a Nawab regarding the division of the estate. When he agreed to so arbitrate no stipulation was made for his remuneration, but in view of the task involved he was paid a certain amount by way of reward for his services :

Held, that the payment was a receipt of a casual and non-recurring nature and was exempt from assessment under Section 4 (3) (vii) of the Income-tax Act,

LEACH, C. J.—*There can be no rule laid down with regard to what is of a casual and non-recurring nature. Each case must be decided on its particular facts.*

Case referred to the Madras High Court by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by Section 92 of the Income-tax (Amendment) Act (VII of 1939) in Application No. 66 R.A. No. 15, Madras of 1942-43 on its file for decision on the following question of law, namely :—

“Whether the sum of Rs. 7,000 being the assessee's share of second instalment of the remuneration of the arbitrator was not assessable as income, profit and gains of the assessee during the previous year and whether the assessee is entitled as regards this income to exemption under Section 4 (3) (vii) of the Act as receipt not being receipts arising from business or the exercise of a profession, vocation or occupation, which are of a casual and non-recurring nature.”

Case Referred No. 18 of 1943.

On the application of the Commissioner under Section 66 (1) of the Income-tax Act, the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. VERMA, (Judicial Member) and P. N. S. AIYAR (Accountant Member) referred the case to the Madras High Court on 24th February, 1943.

STATEMENT OF CASE.

“The Commissioner of Income-tax, Madras, has asked us to refer the following question of law to the High Court of Judicature at Madras :—

“Whether the sum of Rs. 7,000 being the assessee's share of second instalment of the remuneration of the arbitrator was not assessable as income, profit and gains of the assessee during the previous year and whether the assessee is entitled as regards this income to exemption under Section 4 (3) (vii) of the Act as receipt not being receipts arising from business or the exercise of a profession, vocation or occupation which are of a casual and non-recurring nature.”

The respondent to this has filed a reply and has contested that the question formulated by the applicant is one of law. It is submitted by the respondent that it is a question of fact. We have heard the parties and have come to the conclusion that this question is one of law and a fit one to be stated to the High Court for their opinion and we therefore proceed to submit the following statement of the case to the High Court for their opinion under Section 66 (1) of the Indian Income-tax Act.

2. The respondent to this application appealed before the Income-tax Appellate Tribunal against the order of the Appellate Assistant Commissioner, Madras. The respondent had prayed that the sum of

Rs. 7,000 which has been included by the officers below in the assessment was not an income arising from a trade or business and was also of a casual and non-recurring nature and as such exempt under Section 4 (3) (vii) of the Act. This Bench of the Tribunal came to the conclusion that the contention was right and that the sum of Rs. 7,000 received a remuneration for management and arbitration could not be said to arise from the carrying on of a business, profession, vocation or occupation and was an income casual in its nature and was not liable to tax being exempt under Section 4 (3) (vii) of the Income-tax Act. The Appellate Assistant Commissioner, it may be pointed out, by a supplementary order, dated 15th November 1941, considered the question and this was duly considered by us.

3. One Nawab C. Abdul Hakim left considerable estate, and on his death disputes arose among his various heirs regarding the division of the estate. The administration of the late Nawab's property was entrusted to 5 gentlemen of whom the respondent is one. It appears that the preliminary award given by the arbitrators was accepted by the High Court which by their order fixed a remuneration of Rs. 87,000 to be paid to the five arbitrators on the percentage basis. A sum of Rs. 25,000 was paid in pursuance of the order in the accounting year 1938-39. The respondent received Rs. 5,000 in 1938-39 which was subjected to assessment in the year 1939-40. The contention of the respondent in respect of the assessment year 1939-40 was rejected by the Department and in respect of the assessment year with which we are concerned, a sum of Rs. 7,000 was received by the respondent and the same contention was repeated. The principal grounds relied on by the respondent were that (1) it was not income arising from any business or the exercise of a profession, vocation or occupation and (2) that it was income of a casual and non-recurring nature. The Commissioner of Income-tax it may perhaps be mentioned conceded to the first in his order in review in respect of the assessment year 1939-40 and regarding the second point he held that the income under dispute was not of a non-recurring nature as he is to get similar remunerations in future. It was contended before us that at the time when the arbitrators took up the work, there was no agreement between the heirs of the late Nawab and the arbitrators that the arbitrators should be recompensed; and that the remuneration was fixed by the High Court and amounted merely to a short windfall, and so not liable to be taxed. Mr. Justice Gentle who passed the order on 21st October 1938 in C. S. No. 86 of 1938 observed as follows:—

“the arbitrators not only acted as such, they have also negotiated and transacted on behalf of the family and on behalf of the estate with

creditors and debtors. As a result debts due to the estate have been paid which otherwise would not have been realised and reductions have been made in debts owing to creditors. They have acted not only as arbitrators but as *de facto* administrators of the estate."

The decision of the Allahabad High Court in the case of *Chunni Lal Kalyan Das*¹ was relied on by the Appellate Assistant Commissioner and the following observation was quoted by the Appellate Assistant Commissioner:—

"In taking the view we do, we found ourselves mainly upon the use of the word 'nature' in the exemption. The word is not 'occurrence.' If the language were 'a casual or non-recurring occurrence,' there would be much to be said for the contention of the assessee. But the expression 'nature' appears to us to be a word used independently of the accident of the event happening in fact once only or more often in a fortunate year. It connotes a class of dealing which might occur only once, but which might occur several times. Now the adventure of a businessman who is enabled through his business associations to negotiate a large transaction and thereby to earn a heavy commission, may undoubtedly be in fact non-recurring in the sense that so successful an adventure would not be likely to occur again. But on the other hand it is a class of transaction which might occur to any such businessman once only or half a dozen times again, during the course of the year."

The Appellate Assistant Commissioner came to the conclusion that the respondent was "a graduate and was a member of the Provincial Legislature, and a person of influence and held in regard by the members of his community and has had large experience in business, and on account of these qualifications he was selected as an arbitrator for the administration of the Nawab's estate." It was conceded by the Appellate Assistant Commissioner that such duties were performed by him in the past by way of social obligation and *it is quite probable that he might be called upon in future to hold similar office* and he thought that the remuneration he received as an arbitrator might happen again. The Tribunal gave its reasons for coming to the conclusion in its order, dated 11th August 1942. This Bench of the Tribunal simply relied on the case *Shaw Wallace & Co.*² It does not appear to us that an arbitration of this nature can be said to be carrying on of a business or the exercise of a profession, vocation or occupation. The sum has been awarded in an exceptional case for rendering services in the arbitration on account of the confidence that the parties reposed in the arbitrators and the income appears to us to be merely casual and not liable to recur. The question, according to us, being one of law

(1) (1924) 1 I.T.C. 419.

(2) (1932) 6 I.T.C. 178.

we submit the case to the High Court for its opinion under Section 66 (1) and the question is stated in the following form :—

“ Whether the sum of Rs. 7,000 being the assessee's share of second instalment of the remuneration of the arbitrator was not assessable as income, profit and gains of the assessee during the previous year and whether the assessee is entitled as regards this income to exemption under Section 4 (3) (vii) of the Act as receipt not being receipts arising from business or the exercise of a profession, vocation or occupation, which are of a casual and non-recurring nature.”

[The opinion of the Appellate Tribunal as stated in the Judgment of the Tribunal delivered under Section 33 of the Act was as follows.]

“ The contention of the appellant was that it was a casual income exempt under Section 4 (3) (vii) of the Income-tax Act but this was negatived. In the “ previous year ” the petitioner received another instalment, a sum of Rs. 7,000, as his share and it is again contended that this sum is exempt for the following reasons :—

(i) that it was not income arising from any business or the exercise of a profession, vocation or occupation, and

(ii) that it was income of a casual and non-recurring nature.

It may be pointed out that there is no *res judicata* or *estoppel* in the income-tax proceedings and what was decided in the previous assessment will not debar us from considering if the amount appears to be exempt from taxation. The Appellate Assistant Commissioner in repelling the argument of the appellant observed as follows :—

“ In this case the petitioner is a graduate and was a member of the Provincial Legislature. He is a person of influence and held in regard by the members of his community and has had large experience in business. On account of these qualifications he was selected as an arbitrator for the administration of the Nawab's estate. Admittedly he has performed such duties in the past by way of social obligations and it is quite probable that he might be called upon in future to hold similar office. Therefore, the remuneration he received as an arbitrator in this case might happen again. In this sense the income is of a recurring nature and does not come under the exemption contemplated in Section 4 (3) (vii) of the Act. The amount has been rightly included in the assessment.”

The Appellate Assistant Commissioner has relied on the decision of the Allahabad High Court in the matter of *Chunni Lal Kalyan Das*¹ and the pertinent observation is quoted in his order. The Departmental Representative has further referred us to the case reported in 14 Tax Cas. 684 (*The Balcrow Land Trust, Ltd. v. The Commissioners of*

(1) (1924) 1 I.T.C. 419.

Inland Revenue) and has contended that this income should be deemed to be in the nature of vocation and he tried to bring this income under Section 10 of the Income-tax Act. Lastly, he thinks that in any case it should come under Section 12 of the Income-tax Act being income from other sources. Their Lordships of the Privy Council in the case of *Shaw Wallace & Co.*¹, observed as follows :—

“Income in the Indian Income-tax Act connotes a periodical monetary return, ‘coming in’ with some sort of regularity or expected regularity, from definite sources not necessarily continuously productive whose object is the production of a definite return excluding anything in the nature of windfall.”

The appellant was appointed an arbitrator in this case and there is no instance of his having had any remuneration in any arbitration. It seems to us a far-fetched idea that an arbitration of this nature in the family dispute by friends of the family can be said to be carrying on of a business, profession or vocation. It is a particular position in which a person is placed that calls for his offices as a settler of dispute and there cannot be any professional arbitration. Each case is a matter of confidence and not because of a man possessing certain degrees and being member of a Legislative Assembly that he may be called upon to arbitrate. The position or the influence possessed by the appellant may not attract other persons with whom he is not connected. The source of income should have a sort of continuity and should not be casual. If the object was to tax all sorts of income this exemption under Section 4 (3) (vii) of the Income-tax Act exempting casual income should not have been enacted. The sum of Rs. 87,000 between five persons has been awarded in an exceptional case for rendering services in the arbitration on account of the confidence that the parties reposed in the arbitrators and the income appears to us to be merely casual and not liable to recur in the manner as observed by the Appellate Assistant Commissioner. We think this receipt of remuneration should not be taxed as the appellant's income.

8. The result is that we allow this claim of Rs. 7,000 and order it to be deleted from the assessable income of the appellant and confirm the order of the Appellate Assistant Commissioner in regard to the disallowance of the claim of loss of Rs. 10,886 in a partnership concern.”

K. V. Sesha Aiyangar, for the Commissioner.

G. Srinivasan and *G. Devarajan*, for the assessee.

JUDGMENT.

LEACH, C.J.—The assessee is a merchant dealing in hides and he carries on his business in the City of Madras. In the year 1938 one Nawab C. Abdul Hakim died, leaving a large estate. Disputes arose

among the heirs with regard to the division of the properties left by the Nawab. The result was that the heirs chose five gentlemen of the same community to act as arbitrators and assist in the distribution of the assets. The assessee was one of the five gentlemen, who have been referred to in these proceedings as "the arbitrators." The arbitrators did a considerable amount of work in connection with the administration of the estate, and when at a later stage there were proceedings in this Court in regard to the partition, Gentle, J., decided that a sum of Rs. 87,000 (arrived at on a percentage basis) should be divided among the five arbitrators. The assessee's share came to Rs. 17,400. It was not possible to pay to the arbitrators the full amount at once and they received their shares in instalments spread over a number of years. The second instalment which was paid to the assessee was Rs. 7,000 and it was paid during the year of account 1940-41. The Income-tax Officer decided that the assessee was liable to income-tax in respect of this sum and consequently assessed him thereon. The Appellate Assistant Commissioner agreed with the Income-tax Officer, but the Income-tax Appellate Tribunal, Calcutta Bench, reversed the orders of the Income-tax authorities on the ground that the payment represented a receipt of a casual and non-recurring nature. At the instance of the Commissioner of Income-tax, the Tribunal has referred to this Court for decision the following question :

"Whether the sum of Rs. 7,000 being the assessee's share of second instalment of the remuneration of the arbitrator was not assessable as income, profit and gains of the assessee during the previous year and whether the assessee is entitled as regards this income to exemption under Section 4 (3) (vii) of the Act as receipt not being receipts arising from business or the exercise of a profession, vocation or occupation, which are of a casual and non-recurring nature."

In the course of the arguments certain English cases have been referred to, but we do not regard them as being really helpful because the schemes of the two Acts are not identical. In fact there is considerable divergence here. Under sub-section (1) of Section 4 of the Indian Act, the tax is levied upon the income, profits and gains of the previous year. Sub-section (3) says that the income, profits or gains falling within specified classes shall not be included in the total income of the person receiving them. Clause (vii) exempts:

"any receipts not being receipts arising from business or the exercise of a profession, vocation or occupation, which are of a casual and non-recurring nature, or are not by way of addition to the remuneration of an employee."

In deciding whether this sum of Rs. 7,000 is taxable the Court can only have regard to the provisions of Section 4 of the Act.

Now it is clear that the Rs. 7,000 is not a receipt arising from the exercise of a profession, vocation or occupation. As we have already pointed out, the assessee is a merchant dealing in hides and his agreement to act as an arbitrator was entirely apart from his business. When he agreed to assist in settling the differences of the heirs of the Nawab no stipulation was made for remuneration. He obviously consented to act as he was a friend of the family; but it turned out that the task involved far more time than was anticipated and this was the reason why Gentle, J., decided to grant the arbitrators a reward for their services. There was no obligation to remunerate the arbitrators and if Gentle, J., had refused to sanction remuneration nothing would have been payable. In our opinion the facts of this case show that this is a receipt of a casual and non-recurring nature. It has been said that the assessee may act as an arbitrator in another case. That may be so; but he is not a professional arbitrator and it is very unlikely that he will be called upon to act in a case like the one referred to. There can be no rule laid down with regard to what is of a casual and non-recurring nature. Each case must be decided on its particular facts. We think that in the circumstances of this case the Income-tax Appellate Tribunal took the correct view. Therefore the answer to the question referred is that the Rs. 7,000 is not assessable. The assessee has succeeded and he is entitled to his costs, Rs. 250.

Reference answered accordingly.

[IN THE MADRAS HIGH COURT.]

V. RAMASWAMY AYYANGAR AND ANOTHER
v.

COMMISSIONER OF INCOME-TAX, MADRAS.

SIR LIONEL LEACH, C.J. and LAKSHMANA RAO, J.

October 22, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (xii)—BUSINESS EXPENDITURE—EXECUTORS—EXPENDITURE INCURRED IN PAYMENT OF DEATH DUTY AND FOR OBTAINING PROBATE AND LETTERS OF ADMINISTRATION—WHETHER ALLOWABLE DEDUCTION.

A Chettiar who had business assets in British India, Ceylon, Federated Malay States and Cochin China died leaving a will. The will was proved in British India and letters of administration were obtained in Colombo. Under the laws of Ceylon, Federated Malay States and Cochin China the executors had to pay death duties. The executors sought to deduct from the income of the estate of the testator the expenditure incurred in payment of death duties and in obtaining probate and letters of administration :

Held, that the expenditure incurred in payment of death duties and in obtaining probate and letters of administration was not deductible under Section 10 (2) (xii) of the Income-tax Act.

P. C. Mallick and D. C. Aich, In re [1936] (4 I.T.R. 369) affirmed by the Privy Council in [1938] (2 Cal. 214; 6 I.T.R. 206), referred to.

Case referred to the High Court by the Income-tax Appellate Tribunal, Calcutta Bench, under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by Section 92 of the Income-tax (Amendment) Act VII of 1939 in Application No. 66 R. A. No. 4 Madras of 1942-43 on its file for decision on the following question of law, *vis.*, "Whether expenditure incurred in connection with death duty, for obtaining letters of administration and for obtaining probate of the will of the deceased owner, is not deductible under Section 10 (2) (xii) of the Act?": Case Referred No. 15 of 1943.

On the application of the assessee under Section 66 (1) of the Indian Income-tax Act (XI of 1922), the Income-tax Appellate Tribunal, Calcutta Bench, consisting of R. P. VERMA (Judicial Member) and P. N. S. AIYAR (Accountant Member) referred the case to the Madras High Court on 19th December 1942.

STATEMENT OF CASE.

"This is an application praying for reference to the High Court of Judicature at Madras. The questions stated by the applicant are:—

(a) Whether the death duty of \$ 62,450 paid at Saigon and \$ 1,888.69 being legal expenses incurred in that connection are not allowable deduction within the meaning of Section 10 (2) (xii) of the Act.

(b) Whether the expenses of Rs. 311 and Rs. 1,000 incurred in Colombo in connection with the proceedings relating to the death duty are not revenue expenditure allowable under Sec. 10 (2) (xii) of the Act.

(c) Whether the following 4 items of expenditure are not revenue expenditure allowable under Section 10 (2) of the Act:—

- | | | |
|-------------------------------|---|-------------------------------------------------------------------------------|
| 1. Rs. 7,924 legal expenses | } | Incurred for obtaining letters of administration at Colombo by the Receivers. |
| 2. Rs. 588 travelling charges | | |

3. Rs. 8,010 being expenses by Executors for obtaining probate in the Ramnad District Court at Madura.

4. Rs. 2-8-0 being cost of Estate Duty Ordinance book purchased at Kuala Lumpur?

2. The Commissioner of Income-tax, Madras, who is the respondent to this petition states that question of law does not arise to justify a reference to the High Court. According to him the estate duty in question was incurred to secure the right and title to the assets and for the purposes of acquiring the right to carry on the business in all the

future years. They were certainly not laid out or expended wholly and exclusively for the purposes of carrying on the appellant's money-lending or other business which are the subject-matter of the assessment. It is further contended that they were non-recurring and clearly of a capital nature. Reliance is laid on the Madras High Court Order in O. P. 86/42, dated the 20th July 1942, where it has been held by the High Court that the question whether the sum incurred as expenditure is of a capital or of a revenue nature is one of fact.

3. In reply the applicant contends that the Commissioner of Income-tax, Madras, is not correct in saying that the estate duty was paid for the purposes of acquiring the right to carry on the business in all future years. The purpose and the legal obligation of the payment of the duty in question have been set out, it is contended, in paragraphs 5 and 5 (a) of the application, dated the 8th April, 1942, made by the applicant for reference to the High Court. It is submitted that the question whether expenditure compulsorily incurred for carrying on the business and for protecting the stock-in-trade of the foreign business of the deceased person should be reckoned as business expenditure or capital expenditure is a question of law. It is also submitted that the question decided by the High Court and relied on by the Commissioner related to a different set of facts.

4. We have heard the contentions of the parties and have come to the conclusion that in the question raised there is question of law. The Madras High Court's decision referred to above held whether in the facts of that case the estate duty paid in respect of properties purchased in the course of business at Penang in the names of agents who were since dead is an allowable deduction under Section 10 (2) (xii) of the Income-tax Act, was a question of fact. We have taken certain rulings and legal implications into consideration in coming to the findings that the sums in question are not deductible under Section 10 (2) (xii) of the Act.

5. In the case of *P.C. Mullick and Another (Executors) v. Commissioner of Income-tax, Bengal*, reported in [1938] (6 I.T.R. 206), one of the questions mentioned by their Lordships of the Privy Council to have been referred to was:—

“Whether or not the cost of obtaining probate of the will of Akshoy Kumar Ghosh should have been excluded from the chargeable ‘income’ of the assessee, particularly in view of the express provisions in the will that the same shall be payable out of the income?”

6. In coming to the conclusion to which we have come in our order, dated 28th January 1942, we relied on the observation of Lord Russell of Killowen at page 210 which is to the following effect:—

"The payment of the Shradh expenses and the costs of probate were payments made out of the income of the estate coming to the hands of the appellants as executors, and in pursuance of an obligation imposed by their testator."

We therefore consider that the question in the form to be stated is a question of law and we accordingly draw up the statement.

7. The appellant claimed as deduction the following costs in respect of obtaining probate, payment of death duty and obtaining the letters of administration :

(a) Rs. 311 expenses at Colombo in connection with death duty in old agency account.

(b) Rs. 100 expenses at Colombo in connection with death duty in new agency account.

(c) Rs. 7,924 expenses at Colombo for obtaining letters of administration.

(d) Rs. 218 costs of above Estate Duty Ordinance received at Kuala Lumpur.

(e) Rs. 8,010 costs received at Madras for obtaining probate.

(f) \$ 62,450 death duty paid at Saigon.

(g) \$ 1,888.69 legal expenses in regard to payment of death duty at Saigon.

The Income-tax Officer disallowed these expenses as being expenses of a capital nature. The Appellate Assistant Commissioner confirmed the order of the Income-tax Officer disallowing such expenses. The applicant contended that the case reported in [1938] (6 I.T.R. 206) (*P. C. Mullick and Another (Executors) v. Commissioner of Income-tax, Bengal*) is distinguishable inasmuch as the probate charges were held inadmissible in that case because there was a will containing a direction that such charges should be paid out of the income of the estate and it was, therefore, held that the payment was only an allocation by the testator of a part of the income after it has been received by him. We had also before us the case of *P. C. Mallick & D. C. Aich, In re*, reported in [1936] (4 I.T.R. 369) and the reasonings confirmed on appeal in this Privy Council case. The reasoning of the learned Judges of the Calcutta High Court in considering the question was not based upon the distinction sought to be made out by the applicant. Sir Harold Derbyshire, Chief Justice, observed as follows :—

"According to Section 321 of the Succession Act, the expenses of obtaining probate or letters of administration, including the costs incurred for or in respect of any judicial proceedings that may be necessary for administering the estate, shall be paid next after the funeral expenses and death bed charges, so that the cost of probate

normally will be payable out of the general funds of the estate. In my view no deduction should be allowed on the chargeable income in respect of the cost of obtaining probate of the will."

This observation will show that the disallowance was on general law and not on the particular contents of the will. Costello, J., who wrote the concurring judgment observed:—

"It follows, therefore, that there was income coming into the hands of the executors, the present assessee, in such a manner that it became chargeable to tax before any part of that income was expended by the executors either for the purpose of discharging the cost of probate....."

In our opinion therefore, the expenses incurred were of a capital nature and we, therefore, held that they were not admissible deduction in computing the assessable income of the applicant.

8. We accordingly refer the following question of law to the High Court of Judicature at Madras under Section 66 of the Income-tax Act and direct that the papers mentioned in the Index attached be submitted to the High Court:—

"Whether expenditure incurred in connection with death duty, for obtaining letters of administration and for obtaining probate of the will of the deceased owner, is not deductible under Section 10 (2) (xii) of the Act?"

C. Padmanabha Ayyangar, for the assessee.

K. V. Sessa Ayyangar, for the Commissioner.

JUDGMENT.

(Judgment of the Court was delivered by the Honourable the Chief Justice.)

One RM. AR. AR. RM. Arunachalam Chettiar died on the 23rd February 1938 leaving a will. He had assets in British India, Ceylon, Federated Malay States and Cochin China. The will was proved in British India and letters of administration were obtained in Colombo. Under the laws of Ceylon, Federated Malay States and Cochin China the executors were called upon to pay death duties. For the year of assessment 1939-40 the executors sought to deduct from the income of the estate for the year of account the expenses incurred in obtaining probate and letters of administration and also the amount which they had been compelled to pay in death duties. The Income-tax authorities held that these amounts were not deductible and the decision was upheld by the Income-tax Appellate Tribunal, Calcutta Bench. The estate is now in the hands of receivers appointed by the Subordinate Court of Devakotta and at the request of the receivers the Tribunal has

referred to this Court under Section 66 of the Indian Income-tax Act the following question :—

“ Whether expenditure incurred in connection with death duty, for obtaining letters of administration and for obtaining probate of the will of the deceased owner, is not deductible under Section 10 (2) (xii) of the Act ? ”

Clause (xii) of sub-section (2) of Section 10 allows an assessee to deduct “ any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of such business, profession or vocation.” Before the clause was amended by the Indian Income-tax Amendment Act of 1939, it provided for the deduction of expenditure “ (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains.” Before the amendment the Calcutta High Court in *P. C. Mallick and D. C. Aich, In re*¹, held that the cost of obtaining probate of a will could not be excluded from the chargeable income of the executors, and the decision was upheld by the Privy Council in *Prabash Chandra Mullick v. Commissioner of Income-tax, Bengal*², although the judgment of their Lordships laid stress on the wording of the will which directed the executors to pay the probate duty out of the income of the estate.

Mr. C. Padmanabha Ayyangar, on behalf of the receivers, has very rightly conceded that in view of the amendment of the clause he cannot contend that the cost of obtaining probate and letters of administration are deductible ; but he says that the sums paid in death duties in Ceylon, Federated Malay States and French Cochin China are deductible because they were sums paid in order to enable the executors to carry on the testator's business in those countries. We are unable to accept this argument. Only the expenditure laid out wholly and exclusively for the purpose of the business can be deducted and in our judgment it cannot be said that these payments were made wholly and exclusively for the purpose of carrying on the testator's business. A death duty is a duty imposed by a State for the benefit of the State. Whether the business is carried on or not is no concern of the State. The executors had to make the payments because the law demanded that they should. They represented the estate.

The answer to the question referred is that the expenditure incurred in payment of death duties and in obtaining probate and letters of administration is not deductible under Section 10 (2) (xii) of the Act.

The receivers must pay out of the estate the costs of the Commissioner of Income-tax, Rs. 250.

Reference answered accordingly.

(1) (1936) 4 I.T.R. 369.

(2) (1938) 2 Cal. 214 ; 6 I.T.R. 206.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS

v.

KARIM BROS. CHARITY FUND

SIR JOHN BEAUMONT, C. J., and CHAGLA, J.

September 23, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 4 (3) (i)—TRUST—CHARITABLE OR RELIGIOUS PURPOSES—FAMILY CHARITY FUND—PART OF INCOME OF 'TRUST TO BE SPENT FOR POOR OR UNEMPLOYED MEMBERS OF A'S FAMILY AND ON RELIGIOUS OR CEREMONIAL OCCASIONS—WHETHER INCOME EXEMPT FROM TAXATION.

A wakf deed provided inter alia that 34 per cent. of the net income of the trust referred to as the 'Family Charity Fund' should be spent "for the maintenance, support, or well-being of the poor, needy, destitute, distressed, disabled or unemployed members of the families of A, his sons, grandsons and male lineal descendants from generation to generation, including payments in the shape of monthly or periodical doles or pensions or of lump sums on religious or ceremonial occasions." A further 33 per cent. known as 'Education Fund' was to be spent for educational purposes and the remaining 33 per cent. known as the 'Charitable and Religious Fund' was to be used for the relief of the poor members of the Mahomedan community. The Income-tax authorities allowed exemption under Section 4 (3) (i) of the Income-tax Act in respect of the 'Education Fund' and 'Charitable and Religious Fund' but disallowed it in the case of the 'Family Charity Fund'. On a reference under Section 66 (3):

Held, that that portion of the income of the trust which was allocated to the 'Family Charity Fund' was not exempt from taxation under Section 4 (3) (i).

BEAUMONT, C. J.—*Marriage ceremonies cannot be regarded as charitable.*

Case stated under Section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay, Sind and Baluchistan : (Income-tax Reference No. 5 of 1943).

STATEMENT OF CASE.

"My Lords,

Under Section 66 (3) of the Indian Income-tax Act, XI of 1922 (hereinafter referred to as "the Act"), and in compliance with your Lordships' order, dated the 27th March 1941, I have the honour to

refer for your Lordships' decision the question of law stated in paragraph 10 below which has arisen from the assessment of the Trustees of the Ahmed Abdul Karim Brothers Charity Trust (hereinafter referred to as "the assessee") for the assessment year 1938-39.

2. *Facts of the Case.*—The Trust which forms the subject of this reference was established by an indenture dated the 3rd of May 1935. The settlors were three brothers, Ahmed Abdul Karim, Ayoo Abdul Karim and Omar Abdul Karim, who are all sons of Abdul Karim Peermahomed, and three sons of a fourth brother. The Trustees are the three brothers named above and Ahmed Haji Mahomed, the eldest son of the fourth brother.

3. Clause (a) of paragraph 1 of the indenture provides as follows:—

"The trustees shall set apart 34 per cent. of the net income of the Trust premises (hereinafter referred to as "the Family Charity Fund") and shall utilise and spend the same for the maintenance, support or well-being of the poor, needy, destitute, distressed, disabled or unemployed members of the families of the said Abdul Karim Peermahomed, his sons, grandsons and male lineal descendants from generation to generation, including payments in the shape of monthly or periodical doles or pensions or of lump sums on religious or ceremonial occasions provided however that the trustees shall be at liberty to utilise and distribute the said Family Charity Fund for and amongst such members and in such sums or proportions as they, the trustees, shall in their absolute and uncontrolled discretion think fit provided nevertheless that the trustees shall not in any one year give to any one person either at one time or at different times more than 25 per cent. of the amount of the Family Charity Fund for such year or of the amount of accumulations of any preceding or previous year or years."

A further 33 per cent. which is known as the "Education Fund," was to be spent in providing education for members of the Mahomedan community and the remaining 33 per cent. which is known as the "Charitable and Religious Fund," was to be used for the relief of poor Mohamedans and for contributions to religious or charitable institutions. It was further provided that "the Trustees shall have full power and authority in any year or years to increase the proportion of the net income of the trust premises to be set aside and utilised for the "Family Charity Fund" to a maximum of 44 per cent. and if in any year the proportion of the "Family Charity Fund" is increased beyond 34 per cent., the excess shall be taken from the other two funds in equal proportions." A copy of the indenture is annexed as exhibit A,

4. During the years up to 1938-39 the actual receipts and payments of that part of the trust which is known as the "Family Charity Fund" were as follows :—

| Receipts. | Payments. | Balance. |
|-----------|----------------------------------------------------------------------------------------------------------------------------|-------------|
| Rs. | 1935-36 | Rs. |
| 1,871 | nil | 1,871 |
| | 1936-37 | |
| 8,458 | To Bai Mariambai, daughter of Oomar Abdul Karim (who is one of the settlers) for the marriage expenses of her daughter ... | 1,000 |
| | To Bai Mariambai for maintenance allowance ... | 650 |
| | To Abdul Gafur & Abdul Masjid (grandsons of one of the settlers) for boarding fees and books ... | 325 |
| | | <hr/> 1,975 |
| | 1937-38 | 8,354 |
| 9,325 | To Bai Mariambai for maintenance and allowance ... | 600 |
| | To Bai Mariambai for Ramjan ... | 220 |
| | To Abdul Gafur & Abdul Masjid for boarding fees and books ... | 719 |
| | | <hr/> 1,539 |
| | 1938-39 | 16,140 |
| 7,316 | To Bai Mariambai for maintenance allowance ... | 600 |
| | To Bai Mariambai for Ramjan ... | 309 |
| | To Abdul Gafur & Abdul Masjid for boarding fees and books ... | 650 |
| | To Bai Yemna, sister of Ahmed Haji Mahomed (who is one of the settlers for marriage expenses) ... | 1,000 |
| | | <hr/> 2,559 |
| | | 20,897 |

5. For the assessment year 1937-38 the assessees claimed a refund of the tax deducted at source from the dividend income of the trust. The Income-tax Officer allowed a full refund in respect of 66 per cent. of the income, but held that the remaining 34 per cent. which had been allocated to the "Family Charity Fund," was not entitled to exemption. His decision was upheld by the Appellate Assistant Commissioner on appeal. An application was then submitted to the Commissioner

of Income-tax under Section 33 of the Act but he declined to interfere. The assessee did not claim a reference to the High Court in respect of this assessment.

6. For the assessment year 1938-39 the assessee again claimed a full refund under sub-section (3) of Section 4. The relevant portion of this section, as in force during the year 1938-39, reads as follows:—

“(3) This Act shall not apply to the following classes of income:—

(i) Any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purposes, the income applied or finally set apart for application thereto.

* * * * *

In this sub-section “charitable purpose” includes relief of the poor, education, medical relief, and the advancement of any other object of general public utility.”

Following the decision reached in the previous year the Income-tax Officer held that 66 per cent. of the income was exempt from taxation under this section, but he refused to allow a full refund in respect of the remaining 34 per cent. A copy of his order is annexed as exhibit B.

7. The assessee then appealed to the Appellate Assistant Commissioner, A-Range, Bombay, who upheld the decision of the Income-tax Officer. A copy of the Appellate Assistant Commissioner's order is annexed as exhibit C.

8. Thereafter the assessee submitted an application to the Commissioner of Income-tax, Bombay, under Sections 33 and 66 (2) of the Act in which they requested the Commissioner either to revise the Appellate Assistant Commissioner's decision or to make a reference to the High Court. My predecessor however declined to interfere and held that there was no need for a reference. A copy of his order is annexed as exhibit D.

9. Being dissatisfied with my predecessor's decision the assessee submitted an application to the High Court under Section 66 (3) of the Act, and by your Lordships' order, dated the 27th of March 1941 the Commissioner was directed to refer to the High Court the appropriate questions of law arising in the case with his own opinion thereon.

10. *Question for decision.*—In my opinion there is only one question of law which arises in this case, and I think it might be stated as follows:—

Whether that portion of the income of the trust which is allocated to the “family charity fund” is income which is exempt from taxation under the provisions of sub-section (3) (i) of Section 4 of the Act.

11. *Opinion of the Commissioner.*—In *Dr. Umar Bakhsh v. Commissioner of Income-tax, Punjab*¹, a Full Bench of the Lahore High Court held that income from property dedicated to a wakf which was used for the maintenance of the settlor and his children was not income devoted wholly to religious or charitable purposes within the meaning of Section 4 (3) (i) of the Act, and this decision was followed by the Bombay High Court in the case of *Abubaker Abdul Rehman & Others v. Commissioner of Income-tax, Bombay*². They assesseees have however sought to distinguish their case on the ground that under the terms of the indenture the beneficiaries are to be “poor, needy, destitute, distressed, disabled or unemployed.” They claim that this is sufficient to bring their case within the scope of the explanation to Section 4 (3), which states that “‘charitable purpose’ includes relief of the poor, education, medical relief, and the advancement of any other object of general public utility.”

12. As regards the meaning of the words “object of general public utility” I venture to refer to two rulings. In *Trustees of Wernher's Charitable Trust v. Commissioners of Inland Revenue*³ it was held that expenditure incurred on a recreation field for the employees of a public company was not charitable, and in *Commissioner of Income-tax, Bombay v. The Grain Merchants' Association of Bombay*⁴ it was held that money spent for the benefit of a section of the public, namely, those interested in commerce, was not entitled to exemption. In both of these cases the expenditure in question was likely to benefit a considerable number of people who were in no way related to the donors, yet the objects were not considered to be objects of general public utility. I submit that it should follow *a fortiori* that a fund such as the “family charity fund,” which can be used only for the benefit of the family and descendants of a particular individual, cannot be regarded as serving an object of general public utility.

13. I further submit that under the provisions of the indenture, which has been quoted in paragraph 8 above, the income of the “family charity fund” can be used for purposes which are neither religious nor charitable. In this connection I venture to draw attention to three points:—

(1) It is specifically provided that lump sum payments can be made on “religious or ceremonial occasions.”

(2) The settlors are themselves eligible for relief since they are all sons or grandsons of Abdul Karim Peermahomed.

(1) (1931) 5 I.T.C. 402.

(2) (1939) 7 I.T.R. 139.

(3) (1937) 21 Tax Cas. 137 ; 6 I.T.R. 701,

(4) (1938) 6 I.T.R. 427.

(8) Relief can be granted to "unemployed" members of the family who may not be either poor, needy, distressed or disabled.

As regards the third point, the word "unemployed" can be interpreted as including all persons—men, women or children—who are not engaged in an occupation of profit. As will be seen from paragraph 4 above this seems to be the interpretation which has in fact been adopted by the trustees. Up to the end of the year 1938-39 the only persons who had received donations from the fund were women and children who are very closely related to the settlors and trustees. Indeed they are so closely related that the settlors would probably have felt bound to provide for their maintenance from other sources if the "family charity fund" had not been available. I submit that such donations are not "charitable" within the meaning of the section, and that income which can be used for such purposes is not "income derived from property held wholly for religious or charitable purposes."

14. For the above reasons I am respectfully of opinion that the question which has been stated should be answered in the negative."

Sir Jamshedji Kanga with R. J. Kolah, for the assesseees.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

BEAUMONT, C. J.—This is a reference made by the Commissioner of Income-tax under Section 66 (3) of the Indian Income-tax Act, this Court having directed the Commissioner to state the question of law. The question raised is: "Whether that portion of the income of the trust which is allocated to the 'family charity fund' is income which is exempt from taxation under the provisions of sub-section (3) (i) of Section 4 of the Act."

The relevant provisions of Section 4 (3) of the Income-tax Act provide for exemption in the case of any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purpose, the income applied or finally set apart for application, thereto; and then it is provided "In this sub-section 'charitable purpose' includes relief of the poor, education, medical relief, and the advancement of any other object of general public utility." That definition is wider than the legal acceptance of the term "charity" under English case law, which does not include purposes of general public utility.

Now, the trust in this case was made in the year 1935 by certain Mahomedan gentlemen, and it recited that the settlors out of charitable motives and consideration and in order to make a permanent dedication for religious and charitable purposes in manner thereafter appearing were desirous of settling and had agreed to settle as and by way of and

in the nature of a Wakf the property therein described. Then the property is transferred to the trustees ; the trustees are to hold the property and pay expenses, and then it is provided : " The trustees shall set apart 34 per cent. of the net income of the trust premises (hereinafter referred to as ' the Family Charity Fund ') and shall utilise and spend the same for the maintenance, support or well-being of the poor, needy, destitute, distressed, disabled, or unemployed members of the families of the said Abdul Karim Peermahomed, his sons, grandsons and male lineal descendants from generation to generation, including payments in the shape of monthly or periodical doles or pensions or of lump sums on religious or ceremonial occasions." Then it is provided that the trustees are to set aside 33 per cent. of the net income of the fund, which is referred to as " the Education Fund " and apply the same for educational purposes ; and they are to set aside another 33 per cent. of the net income of the fund, which is referred to as " the Charitable and Religious Fund," and utilise the same, amongst other things, for the amelioration, relief or well being of poor, needy, destitute, distressed or disabled members of the Mahomedan community.

The Income-tax Officer has allowed a deduction in respect of the " Education Fund " and " Charitable and Religious Fund ", but in his view, which has been upheld by the Assistant Commissioner, and with which the Commissioner agrees, the " Family Charity Fund " is not, within the meaning of Section 4 (3), held wholly for religious or charitable purposes.

The main difficulty in the way of holding that the objects of this Fund are charitable is the reference to " unemployed members of the families ", and the power to apply the income in lump sums on ceremonial occasions. It is argued that the Court should read " unemployed members of the families " *ejusdem generis* with the words which have gone before, namely, " poor, needy, destitute, distressed, disabled." But it is difficult to assign any meaning to " unemployed members " unless the word " unemployed " goes beyond people who are poor, needy, destitute, distressed, or disabled. And it is pertinent to observe that in the case of the trust for members of the Mahomedan community in general, the " Charitable and Religious Fund ", the words used are exactly the same, except for the omission of the words " or unemployed". So that, the settlors evidently intended that whereas in the case of the " Family Charity Fund " unemployed members of the settlors' families were to be entitled to benefit, in the case of the trust for Mahomedans generally " unemployment " was not to be a ground qualifying for relief. It is rightly contended for the Commissioner that unless one gives some restricted meaning to the word " unemployed " people in

that category do not fall within the concept of charity. Many persons are unemployed, not because they are poor, but because they are wealthy enough not to need employment. If the class of unemployed is confined to those who are poor or needy, the class is superfluous because the poor and needy are included in the earlier words. And if "unemployed members of the families" is held to include only persons who are anxious to be employed, but cannot get employment, one is reading into the clause something which is not there were (*sic*) such a gift shall be regarded as charitable. There is a further difficulty in that the income of this fund may be spent on ceremonial occasions, for example on marriage ceremonies of persons who happen to be unemployed. It is difficult to see how marriage ceremonies can be regarded as charitable.

On these grounds, I think the view of the Income-tax Officer and of the Commissioner that this Fund is not held solely for charitable or religious purposes is correct, and we must answer the question raised in the negative. The assessee to pay costs.

CHAGLA, J.—I agree.

Reference answered in the negative.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS

v.

V. RAMASWAMY IYENGAR AND ANOTHER.

SIR LIONEL LEACH, C.J., and LAKSHMANA RAO, J.

October 22, 1948.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE AMENDMENT IN 1939), SECS. 24-B, 26 (2)—DECREASED LEAVING ASSETS INCLUDING BUSINESS—WHETHER SECTION 24-B APPLIES TO WHOLE ASSESSMENT—WHETHER PROFITS OF BUSINESS CAN BE SEPARATELY ASSESSED ON HEIRS UNDER SECTION 26 (2).

A Nattukottai Chettiar, who had large assets including a money-lending business died in February, 1938, leaving a will appointing executors. Subsequently in a suit among the heirs the Court appointed receivers to administer the estate. The question was whether the entire assessment for the accounting year 1937-38 should be made under Section 24-B or whether the assessment of the income of the business should be made on the heirs under Section 26 (2) and the rest of the income under Section 24 B :

Held, that Section 24-B only supplemented and did not override Section 26 (2) and therefore the profits of the business should be separately assessed on the heirs under Section 26 (2).

Cases referred to :

Commissioner of Income-tax v. Reid (1931) 55 Bom. 312; A.I.R. 1931 Bom. 333; 5 I.T.C. 100.

Maharajadhiraj of Darbhanga v. Commissioner of Income-tax, Bihar & Orissa (1934) I.L.R. 13 Pat. 607; 2 I.T.R. 345; 7 I.T.C. 337; A.I.R. 1934 P.C. 200; 150 I.C. 142; 15 P.L.T. 573; 40 L.W. 337; 67 M.L.J. 422.

Case referred to the Madras High Court by the Income-tax Appellate Tribunal, Calcutta Bench, under Section 66 (1) of the Indian Income-tax Act (XI of 1922) as amended by Section 92 of the Income-tax (Amendment) Act, 1939.

Case Referred No. 16 of 1943.

On the application of the Commissioner under Section 66 (1) the Income-tax Appellate Tribunal consisting of R. P. VERMA (Judicial Member) and P. N. S. ARYAR (Accountant Member) referred the case to the High Court on 19th December 1942.

STATEMENT OF CASE.

" This is an application for reference preferred by the Commissioner of Income-tax, Madras, asking us to refer the following question of law under Section 66 of the Income-tax Act to the High Court of Judicature at Madras.

" Whether in the circumstances of this case the entire assessment has to be made under Section 24-B of the Act or has the assessment to be split up into two portions, one falling under Section 26 (2) and the other falling under Section 24-B of the Act ? "

2. The respondent has submitted his reply under rule 54 of the Tribunal Rules and has stated that the question formulated by the applicant is defective inasmuch as it did not refer to the ownership and assessment of the income which accrued or arose in the year of account after the death of the last male holder of the family, *i.e.*, after *23rd February 1938*. The respondent has formulated the following questions of law :—

(i) Whether the provisions of Section 24-B have nullified the scope and application of Section 26 (2) of the Act (as it stood before the passing of the Amendment Act VII of 1939) in case of business carried on by a person who died in the year of account and whose legal representatives succeeded to and carried on the business ?

(ii) Whether the income accrued or earned after the death of the late single male holder of the family was not the income of the legal representatives of the deceased and whether such income is not separately assessable in the hands of the legal representatives ?

3. The order that has given rise to this reference was passed by this Bench of the Tribunal on the 28th January 1942, and on the facts and circumstances of the case the Bench decided :

(i) that the assessee, RM. AR. AR. RM. Arunachalam Chettiar died on 23rd February 1928 leaving as his heirs his two widows and a widow of his son who predeceased him in 1934.

(ii) that he left a will, dated the 9th January 1938, by which he appointed two of his relatives as executors and empowered them to adopt a son to each of the three widows and directed the executors to act as the guardians of such adopted persons till they became majors and the estate was handed over to them,

(iii) that the will also provided that the share of each such adopted son was a third of the residuary estate after payment of the legacies bequeathed,

(iv) that the executors entered on their duties and began to administer the estate,

(v) that late Umayal Ache, the widow of the son of the said Arunachalam Chettiar, filed a suit in the court of the Subordinate Judge at Devakottah claiming that she had a half interest in the estate left by the late RM. AR. AR. RM. Arunachalam Chettiar as the widow of the predeceased son under the provisions of the Hindu Women's Rights to Property Act (Act XVIII of 1937) and claimed a division of the properties in the share to which she was entitled,

(vi) that in the course of the proceedings in the suit the court of the Subordinate Judge of Devakottah appointed on the 18th August 1938 two receivers to manage the estate and carry on the business pending final disposal of the suit,

(vii) that the notice under Section 22 (2) was served on the executors to the estate of RM. AR. AR. RM. Arunachalam Chettiar of Devakottah on 24th April 1938,

(viii) that the assessment had been made on the receivers on behalf of the estate of the late RM. AR. AR. RM. Arunachalam Chettiar of Devakottah on the 29th March 1939 in respect of the income from the following sources, namely:—

| | Rs. |
|-------------------------------------|----------------------|
| (a) interest on securities | ... 2,200 |
| (b) property | ... 2,522 |
| (c) business (as reduced on appeal) | ... 1,84,092 |
| (d) other sources | ... 484 |
| | <hr/> 1,89,298 <hr/> |

that accrued during the previous year ended 31st March 1938, except in regard to a portion of the business carried on at Kuttalam and Colombo, the previous year of which ended on the 12th January 1938.

4. The Tribunal took the views which are mentioned as follows:—

(a) that on the death of the owner, the late RM.AR. AR. RM. Arunachalam Chettiar, the three widows became the owners and as such they had succeeded to the ownership of the business and as the business was being carried on even after the death of the said Chettiar the provisions of Section 26 (2) became applicable and as such the income of the business for the “previous year” was assessable in the hands of the successors, the widows, as Section 26 (2) was existing long before Section 24-B was enacted.

(b) that the assessment of such income made on the estate is, therefore, not warranted by the Act.

(c) that a fresh assessment will have to be made on the estate for the income from the rest of the sources to which they are liable under Section 24-B ?

5. The question of law which therefore arises is stated as under and is referred to the High Court of Judicature at Madras under Section 66 of the Income-tax Act:—

Question of Law Referred.

“Whether in the circumstances of this case the entire assessment has to be made under Section 24-B of the Act or has the assessment to be split up into two portions, one falling under Section 26 (2) and the other falling under Section 24-B of the Act?”

[The opinion of the Appellate Tribunal as stated in the judgment of the Tribunal delivered under Section 33 of the Act was as follows:]

“4. In the appeal before us it is contended that this order of the Appellate Assistant Commissioner is wrong, the assessment of the income from the sources other than under the head “business” up to 23rd March 1938 only should be made on the estate. The income under these heads arising or accruing after that date should be assessed in the hands of the heirs of the deceased. Further as the heirs are continuing the business of the deceased Chettiar, the provisions of Section 26 (2) do apply and the assessment for the income of this business should be made on the heirs and estate of the said RM. AR. AR. RM. is not liable for an assessment for the year 1938-39 on the income from the business.

5. Section 26 (2) reads: “Where at the time of making an assessment under Section 23 it is found that the person carrying on any business, profession or vocation has been succeeded in such capacity by another person the assessment shall be made on such person succeeding as if he had been carrying on the business, profession or vocation throughout the previous year and as if he had received the whole of the

profits for that year." In this case on the death of the owner the late RM. AR. AR. RM. Arunachalam Chettiar the three widows have become the owners and as such they had succeeded to the ownership of the business, and as the business was being carried on even after the death of the said Chettiar, the provisions of Section 25 (2) become applicable and as such the income of the business for the "previous year" is assessable in the hands of the successors, the widows. The assessment of such income made on the estate is therefore not warranted by the Act. Section 26 (2) was existing long before Section 24-B was enacted; while provision had been made in Section 26 (2) for the assessment of income of a business succeeded to by another person by whatever ways, before the enactment of Section 24-B there was no provision to an assessment of the income of a deceased person from the rest of the sources. Even in this same case if the business had not been continued by the heirs of the deceased the provisions of Section 26 (2) will not apply and the provisions of Section 24-B alone apply. The finding of the Appellate Assistant Commissioner that there has been no succession within the meaning of Section 26 (2) of the Income-tax Act is directly opposed to the ruling in *Maharaja of Darbhanga v. Commissioner of Income-tax, Bihar and Orissa*, 12 Patna 5, confirmed by the Privy Council in 13 Patna 607, that this section applied to all kinds of succession and is not restricted to cases of succession *inter vivos*.

6. For the reasons stated above we hold that the assessment made on the estate of the late RM. AR. AR. RM. Arunachalam Chettiar in respect of the income from the business carried on by him during the part of the "previous year" is not valid and the assessment of such income should be made on the successors to that business who were found to be carrying on that business at the time of making the assessment. The assessment made on the estate inclusive of this income is, therefore, cancelled. A fresh assessment will have to be made on the estate for the income from the rest of the sources to which they are liable under Section 24-B, the income accrued till the date of death of the said RM. AR. AR. RM. Arunachalam Chettiar. The income that arose after the death of the said Arunachalam Chettiar belonged to his heirs and as such is assessable in their hands.

7. The second objection raised whether the remittance of Rs. 85,000 is out of capital or profit does not now arise for consideration in this appeal as this objection is raised in connection with the assessment of the income from the business for which by their order it is held that the appellants are not liable.

8. The result is the appeal is accepted."

K. V. Sessa Ayyangar, for the Commissioner.

C. Padmanabha Iyengar, for the assesseees.

JUDGMENT.

LEACH, C. J.—In *Commissioner of Income-tax v. Reid*¹, which was decided on the 3rd October, 1930, the Bombay High Court held that the Indian Income-tax Act contained no provision under which the estate of a deceased person could be taxed. The definition of “assessee” under Section 2 (2) of the Act only applied to a living person. In *Maharajadhiraj of Darbhanga v. Commissioner of Income-tax, Bihar and Orissa*², which related to an assessment made in the year 1929-30, the Privy Council held that Section 26 (2) applied to a person who succeeded to the business of a deceased person and therefore the successor could be taxed in respect of the income obtained from the business in the year of succession. On the 11th September, 1933, the Legislature inserted Section 24-B. Stated broadly, the question which arises here is whether Section 24-B overrides Section 26 (2) and requires, in the case of a person dying leaving a business, the assessment to be made on his executor, administrator or other legal representative, as if he had not died.

This reference arises out of the assessment made on the Receivers of the estate of one RM. AR. AR. RM. Arunachalam Chettiar, who died on the 28rd February 1938. He was survived by his two wives and the widow of a predeceased son. He left a will and therein appointed executors. The estate is now being administered by the Court of the Subordinate Judge of Devakottai, who appointed the Receivers. In Appeals Nos. 321 of 1940, and 3, 104 and 239 of 1941, this Court had to decide the rights of the widows and the son's widow. The deceased had large assets which included a money-lending business in British India with branches in Ceylon, the Federated Malay States and in French Cochin China. The decision of this Court, so far as it affects the present case, was that the deceased's widows and the son's widow were entitled to the moveable assets in British India, but that the son's widow did not share in the moveable assets outside British India. The three ladies can be regarded as the successors to the deceased's business, although not in equal shares.

In the present case the year of account is from the 12th April 1937 to the 12th April 1938. The Income-tax Officer held that the Receivers were to be assessed to income-tax and super-tax in respect of the whole of the estate, including the profits of the business. The Receivers contended that the profits of the business should be separately

(1) (1930) 8 I.L.R. 55 Bom. 312.

(2) (1934) 2 I.T.R. 345 ; L.R. 61 I.A. 312.

assessed and the tax levied on the widows under Section 26 (2). The Appellate Assistant Commissioner upheld the order of the Income-tax Officer, but on appeal to the Income-tax Appellate Tribunal, Calcutta Bench, the Receivers' contention was accepted. At the request of the Commissioner of Income-tax the Tribunal has referred the following question under Section 66 of the Income-tax Act :—

“ Whether in the circumstances of this case the entire assessment has to be made under Section 24-B of the Act or has the assessment to be split up into two portions, one falling under Section 26 (2) and the other falling under Section 24-B of the Act ? ”

The argument advanced on behalf of the Commissioner is that Section 24-B is self-contained and is wide enough to cover every case where a person liable to income-tax dies during the year of account. The section may be self-contained, but this does not mean that it overrides Section 26 (2). Sub-section (2) of Section 26 was amended in 1939, but the Court must have regard to its provisions before the amendment. It then read as follows :—

“ Where, at the time of making an assessment under Section 23, it is found that the person carrying on any business, profession or vocation has been succeeded in such capacity by another person, the assessment shall be made on such person succeeding, as if he had been carrying on the business, profession or vocation throughout the previous year, and as if he had received the whole of the profits for that year.”

As we have already pointed out, in *Maharajahdhiraj of Darbhanga v. Commissioner of Income-tax, Bihar and Orissa*¹, the Privy Council held that this provision allowed the tax to be levied on the person who succeeded to a business on the death of the owner. In our judgment Section 24-B was inserted in order to supplement Section 26 (2) and to avoid the defect pointed out by the Bombay High Court. If the Legislature had intended Section 24-B to override Section 26 (2), as interpreted by the Privy Council, surely it would have said so. As Section 24-B left Section 26 (2) untouched, we consider that Section 26 (2) must be applied in a case of succession to a business by death and the tax levied on the successor as if he had carried on the business throughout the previous year. This means that we agree with the decision of the Appellate Tribunal and we answer the question referred accordingly.

The respondents are entitled to their costs, Rs. 250.

Reference answered accordingly.

(1) (1934) 2 I.T.R. 345; L.R. 61 I.A. 312.

[IN THE PRIVY COUNCIL.]

THE PATIALA STATE BANK

v.

COMMISSIONER OF INCOME-TAX, BOMBAY.

LORD ROMER, LORD PORTER, LORD CLAUSON,
SIR GEORGE RANKIN and SIR MADHAVAN NAIR.

July 8, 1943.

GOVERNMENT TRADING TAXATION ACT (III OF 1926), SEC. 2—INDIAN STATE CARRYING ON BANKING BUSINESS IN STATE—INCOME DERIVED IN BRITISH INDIA FROM SALE OF INVESTMENTS AND PROPERTY TAKEN OVER FROM DEBTORS—WHETHER LIABLE TO INDIAN INCOME-TAX—SCOPE OF SEC. 2—INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 3 & 4.

Section 2 of the Government Trading Taxation Act, 1926, is not confined in its operation to trades or businesses carried on in British India, and therefore if an Indian State carries on a banking business, the income, profits and gains of that business which accrue, arise or are received in British India would be liable to taxation under the Indian Income-tax Act, even though the head office and all the branches of the bank are situated in the State and it does not carry on any banking business in British India.

Income arising from property situated in British India which such a bank has taken over from one of its debtors residing in the State in part satisfaction of a loan is liable to assessment in British India. Profits received in British India from the sale of investments made in the course of the banking business would also be liable to assessment in British India.

Judgment of the Bombay High Court in *Patiala State Bank, In re* [1941] (9 I.T.R. 95) affirmed.

Case referred to :—

In the matter of Ram Prasad (1930) I.L.R. 52 All. 419.

P. C. Appeal No. 44 of 1942,

Cyril King and *F. S. Scrimgeour*, for the Appellant.

F. Millard Tucker and *W. Wallach*, for the Respondent.

JUDGMENT.

LORD ROMER.—The Patiala State Bank (the appellant in this case) is owned and controlled by the Maharaja of Patiala who constitutes the Government of that State. The head office and all the branches of

the bank are situated in the State and it does not carry on any part of its business in British India. But in the year ending 31st March, 1935, the bank collected and received in British India through the hands of its agents sums representing the interest on certain Government of India securities that it had acquired in the course and for the purposes of its business. In the same year, it also received in British India, through its agents there, a substantial sum of money representing the profits accruing to it in respect of the sale at a profit of various investments similarly acquired. It is not and it cannot be disputed that all these sums of money represented profits or gains of the appellant's banking business for the year in question. In these circumstances the Senior Income-tax Officer, Non-Resident Refund Circle, Bombay, in the month of August, 1937, caused an assessment to be made on the bank for the year 1935-36 in respect of the said sums (and of certain other small sums representing income of the bank received in British India in the year ending 31st March, 1935) after allowing various permissible deductions.

In making this assessment the Income-tax Officer purported to be acting under the provisions of the Government Trading Taxation Act, 1926 (III of 1926). The preamble to the Act is in the following words:—

“Whereas it is expedient to determine the liability to taxation for the time being in force in British India of the Government of any part of His Majesty's Dominions, exclusive of British India, in respect of any trade or business carried on by or on behalf of such Government; It is hereby enacted as follows :”

The material section of the Act is the second which runs as follows :—

“2. (1) Where a trade or business of any kind is carried on by or on behalf of the Government of any part of His Majesty's Dominions, exclusive of British India, that Government shall, in respect of the trade or business and of all operations connected therewith, all property occupied in British India and all goods owned in British India for the purposes thereof, and all income arising in connection therewith, be liable—

(a) to taxation under the Indian Income-tax Act, 1922, in the same manner and to the same extent as in the like case a company would be liable;

(b) to all other taxation for the time being in force in British India in the same manner as in the like case any other person would be liable.

(2) For the purposes of the levy and collection of income-tax under the Indian Income-tax Act, 1922, in accordance with the

provisions of sub-section (1), any Government to which that sub-section applies shall be deemed to be a company within the meaning of that Act, and the provisions of that Act shall apply accordingly.

(3) In this section the expression 'His Majesty's Dominions' includes any territory which is under His Majesty's protection or in respect of which a mandate is being exercised by the Government of any part of His Majesty's Dominions."

The question to be decided upon this appeal is whether the section applies to the appellant bank. It is conceded that the Patiala State is a State under His Majesty's protection and is therefore within His Majesty's Dominions for the purposes of the section. But the appellant contends that the section only applies to cases where the trade or business in question is carried on in British India. If the section does apply to the bank, then by virtue of sub-section (1) (a) all income arising in connection with its trade or business is liable to taxation under the Indian Income-tax Act, 1922, in the same manner and to the same extent as in the like case a company would be liable. It is therefore desirable to state what are the relevant provisions of the Income-tax Act, 1922, applicable to a company "in the like case." They are as follows :

"Section 2.—(4) 'business' includes any trade, commerce, or manufacture or any adventure or concern in the nature of trade, commerce or manufacture.

Section 3.—Where any Act of the Indian Legislature enacts that income-tax shall be charged for any year at any rates or rate applicable to the total income of an assessee, tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of, this Act in respect of all income, profits and gains of the previous year of every individual, company, firm and Hindu undivided family.

Section 4.—(1) Save as hereinafter provided, this Act shall apply to all income, profits or gains, as described or comprised in Section 6, from whatever source derived, accruing or arising, or received in British India, or deemed under the provisions of this Act to accrue, or arise, or to be received in British India.

Section 6.—Save as otherwise provided by this Act, the following heads of income, profits and gains, shall be chargeable to income-tax in the manner hereinafter appearing, namely :—

* * * * *

(iv) Business.

Section 10.—(1) The tax shall be payable by an assessee under the head 'Business' in respect of the profits or gains of any business carried on by him,"

In the month of October, 1937, the bank appealed against the assessment that had been made upon it, and after some proceedings had taken place before the Assistant Commissioner and the Commissioner which need not be further mentioned, the Commissioner, upon the application of the bank made under Section 66 (2) of the last mentioned Act, referred to the High Court for its decision seven questions of law of which only the following are now material :

“(1) Whether the Government Trading Taxation Act (III of 1926) is applicable to the Patiala State Bank rendering it liable to taxation under the Indian Income-tax Act, 1922 ?

(3) Whether the property situate at Mussoorie taken over by the Patiala State Bank from its debtor, a subject of the Patiala State, in part satisfaction of a loan advanced to him, is property occupied in British India for the purposes of its trade or business in British India within the meaning of Section 2 of the Government Trading Taxation Act and whether all income arising from such property is liable to assessment by virtue of the provisions of the said Act ?

(4) Whether the sum of Rs. 66,720 received by the Patiala State Bank on the sale of its investments during the year 1934-35 being the excess realized by it over the cost price of such investments, which has been included under the heading of profits in the relative profit and loss accounts and balance sheet is assessable to income-tax ?

(5) Whether the income received by the Patiala State Bank from its investments in British India constitutes income arising in connection with a trade or business carried on in British India within the meaning of Section 2 of the Government Trading Taxation Act and is therefore liable to assessment to income-tax ?

(7) Whether the assessment to income-tax and super-tax for the year 1935-36 on the Patiala State Bank is a legal and valid assessment ? ”

Of these questions, No. (3) requires a word of explanation. The property in question produced no income in the year ending on the 31st March, 1935, and was not, therefore, referred to in the assessment for the year 1935-36, that is alone the subject matter of these proceedings. The question, however, would or might arise in subsequent years of assessment, and accordingly by a consent order passed by the High Court it was agreed that the present appeal should be argued and decided on the footing that income from such house property is in fact included in the assessment, the subject of the present appeal. In the circumstances and in order to save expense their Lordships are willing that the appeal should be dealt with on this footing.

The Commissioner, as required by Section 66 (2) of the Income-tax Act, stated his own opinion upon the questions set out above, and upon each of them his opinion was adverse to the contentions of the bank. In particular he rejected its contention that is implied in questions (3) and (5) that the Government Trading Taxation Act only applies to a Government carrying on a trade or business in British India.

On the 8th October, 1940, the reference came before the High Court and was heard by Sir John Beaumont, C. J., and Kania, J. At the hearing before them a contention was put forward on behalf of the bank that does not appear to have been relied upon before the Commissioner. It was that the Act of 1926 was altogether invalid as having been *ultra vires* the Government of India. This contention, which was described by the Chief Justice as being the principal point argued before them and the only question of substance in the case, failed, as might have been expected, to commend itself to the Court, and was very properly abandoned by Mr. King in his address to their Lordships on behalf of the bank. But it was strongly urged before their Lordships, as it was before the High Court, that the Act of 1926 only applies to a trade or business carried on in British India. The contention had been advanced successfully before the High Court of Allahabad in the case *In the matter of Ram Prasad*¹. It was, however, rejected by the High Court in the present case. "I can see," said Beaumont, C.J.:

"no justification for the view.....that the Act is confined to business carried on in British India. It seems to me that the title, the preamble and the operative part of Section 2 make it perfectly clear that it applies to every case in which the Dominion Government is carrying on a business, and when that happens, the Dominion Government is liable to Indian Income-tax, as though it were a company."

Kania, J., expressed himself to the same effect. The High Court accordingly answered the first question in the affirmative. Having done so, they found no difficulty in answering questions (3), (4), (5) and (7). After referring to the provisions of the Income-tax Act of 1922 the Chief Justice said this:

"The effect of the charging sections, Sections 3 and 4, is to render the income, profits and gains of a company liable to British Indian income-tax, if such income, profits and gains accrue or arise or are received in British India. So that Act III of 1926 comes to this: that where a Dominion Government is carrying on a business anywhere, it is liable to British Indian income-tax in respect of the income, profits and gains of that business which accrue or arise or are received in British India."

(1) (1929) I.L.R. 52 All. 419.

As regards question (3) it was accordingly held by the Court that any income derived from the property therein mentioned was income arising in connection with the business of the bank and would fall to be taxed. It was, however, held by the Court that the property was not property occupied for the purposes of the business. Question (4) was also answered in the affirmative, as was question (5) so far as it asked whether the income therein mentioned was liable to assessment to income-tax. It necessarily followed that question (7) was also answered in the affirmative. In the result a formal order dated the 8th October, 1940, was drawn up embodying the answers given by the Court upon the reference. It is from that order that the bank, having obtained the necessary certificate from the High Court under Section 66-A (2), now appeals to His Majesty in Council.

In their Lordships' opinion the answers which the High Court gave to the questions referred to them are plainly right, as is the reasoning upon which these answers were based. There are no words to be found in the Act of 1926 confining the operation of Section 2 to trades or businesses carried on in British India. The words of the section are quite general in their terms, and their Lordships are quite unable to find any reason whatever for introducing into the section by implication the qualification for which the appellant bank contends. The section therefore applies to the business of the bank although it is carried on exclusively in the State of Patiala. That being so it follows that the assessment complained of is a valid assessment, inasmuch as all the items affected by it represent income, profits or gains of the said business received in British India, and are, therefore such as would have been taxable under the Act of 1922 if received by a company "in the like case."

For these reasons, their Lordships will humbly advise His Majesty that the appeal should be dismissed. The appellant must pay the respondent's costs of the appeal.

Appeal dismissed.

SUPPLEMENT
TO
THE
INCOME TAX REPORTS
VOLUME XI
CONTAINING
SELECT ENGLISH CASES.

[IN THE COURT OF APPEAL.]

WALES v. TILLEY.

LORD GREENE, M. R., MACKINNON, L. J., GODDARD, L. J.

May 6, 7, 18, 1942.

INCOME TAX—DIRECTOR OF COMPANY—AGREEMENT FOR SALARY AND PENSION—SUBSEQUENT AGREEMENT TO COMMUTE RIGHTS BY LUMP SUM IN TWO INSTALMENTS—PAYMENTS ASSESSABLE AS INCOME—INCOME TAX ACT, 1918 (8 & 9 GEO. 5, c. 40), SCHEDULE E.*

A limited company agreed to pay the appellant £ 6,000 a year for acting as managing director, and in the event of his ceasing from any cause to be managing director a yearly pension of £4,000 for ten years. By a subsequent agreement, the appellant released the company from its obligation to pay him a pension and agreed to accept a salary of £2,000 a year in consideration of the company's undertaking to pay him £40,000 in two instalments of £20,000 each:—Held, by GREENE, M. R., and GODDARD, L. J.—MACKINNON, L. J., dissenting—that although, if the agreement had been in two parts: one to serve at a reduced salary for £x and the other to give up pension rights for £y, the latter sum, on that agreement, could not have been described as remuneration for services and would not be taxable under Schedule E; yet, as the consideration of £40,000 was entire and

* In India the law on the question whether such payments are assessable to income-tax is now contained in Section 4 (3) (vii) and in Explanation (2) to Section 7 (1) of the Income-tax Act, and in the decision of the Privy Council in *Shaw Wallace and Co.'s Case* (1932) 59 Cal. 153; 2 Comp. Cas. 276.—Ed.

indivisible it was remuneration for services as a director, could not be capital and was taxable under Schedule E. An apportionment would involve a rewriting of the contract.

GREENE, M.R., *dissented from the view expressed by LAWRENCE, J., the trial Judge, that a sum paid in commutation of a pension was necessarily assessable under Schedule E. Whether it were so or not depended on the construction of the agreement; if the sums were merely paid by way of commutation of a future pension, without reference to or connection with the services rendered, it would not be so taxable.*

Per MACKINNON, L.J., dissenting.—So far as the sum of £ 40,000 was paid for the surrender of the prospective right to the pension, the decision in DEWHURST v. HUNTER [1932] (146 L.T. 510; 16 Tax Cas. 605) made it impossible to hold that this part of that sum was taxable under Schedule E. Accordingly, in his view, the case should go back to the Commissioners for apportionment of the sum of £ 40,000.

DEWHURST v. HUNTER [1932] (16 Tax Cas. 605) distinguished.

Decision of LAWRENCE, J., [1942] (1 All E.R. 455) affirmed.

Cases referred to :

Cameron v. Prendergast (1940) 109 L.J.K.B. 486; 1940 A.C. 549; 23 Tax Cas. 122; 8 I.T.R. Suppl. 75; 10 Comp. Cas. 173.

Dewhurst v. Hunter (1932) 145 L.T. 510; 16 Tax Cas. 605.

Short Bros., Ltd. v. Inland Revenue Commissioners (1927) 136 L.T. 689; 12 Tax Cas. 955.

Appeal from a judgment of Lawrence, J.

The Special Commissioners of Income-tax held that the appellant was not assessable for income-tax on £ 40,000 paid to him as managing director of a company in consideration of his agreeing to accept a lower salary and to forfeit certain pension rights. Lawrence, J., reversed that finding and the appellant appealed. The facts are set out in the headnote and more fully in the judgments.

Tucker, K. C., and Donovan, for the appellant.

The Attorney-General (Sir Donald Somervell, K.O.) and R.P. Hills, for the respondent.

May 18.—LORD GREENE, M.R.—By an agreement of June 28, 1937, the remuneration which the appellant had been receiving as managing director of his company was increased from £2,000 to £6,000 a year, and in the event of his ceasing from any cause whatsoever to be managing director, the company agreed to pay him, as and from the date of cessation, a pension of £ 4,000 a year for ten years, reckoned from the same date. There was no agreement between the parties as to the period for which the appellant should serve and his tenure of office could have been, as it still can be, terminated by either party at

any time on whatever may be reasonable notice. The language of the clause relating to the pension is obscure, and questions might have arisen whether the pension was payable after the death of the appellant if he were to die during his service, or after its cessation. By clause 1 of an agreement of April 6, 1938, the appellant released the company from its obligation to pay him the pension. Clauses 2 and 3 were as follows: "2. Mr. Tilley hereby agrees to serve the company as managing director as from the date of these presents at a reduced salary of two thousand pounds per annum. 3. In consideration of the premises the company will pay to Mr. Tilley the sum of forty thousand pounds by two equal instalments, the first of which shall be paid on April 6, 1939."

The Special Commissioners discharged an assessment made under Schedule E in respect of the sum of £40,000 payable under the 1938 agreement, holding that it was a payment in commutation of the company's liability under the 1937 agreement to pay pension and increased salary, and that it was not income in the hands of the appellant. Lawrence, J., reversed this decision, holding that the payment was expressly made in consideration of the appellant's agreement to serve at a reduced salary. Part of the £40,000 he considered to be payable in commutation of the pension, but he held that as the pension would have been assessable under Schedule E, a sum payable in commutation of it would also be assessable under the same schedule. As will be seen, I agree with the conclusion of Lawrence, J., but I respectfully dissent from his view that a sum paid in commutation of a pension is necessarily assessable under Schedule E. The case of *Short Bros., Ltd. v. Inland Revenue Commissioners*¹ cited by Lawrence, J., does not, in my opinion, support his proposition. Indeed, the Attorney-General on behalf of the Crown did not attempt to support this part of the reasoning of the learned Judge. He preferred to argue that the pension was deferred remuneration, and that the acceptance during the service of a sum in commutation of it was the acceptance of present, in place of deferred, remuneration. If the agreement of 1938 had dealt with nothing but the appellant's salary as managing director, reducing the annual amount and providing for payment of a lump sum in consideration of his acceptance of the reduction, there would, in my opinion, have been no difficulty in the case. If a man agrees to serve in consideration of a lump sum and no periodical salary or a small periodical salary, the lump sum is just as much remuneration and taxable as such as a periodical salary or a larger periodical salary would have been (*Prendergast v. Cameron*)². Indeed, the only real argument that was

(1) (1927) 12 Tax Cas. 955.

(2) (1940) 8 I.T.R. Suppl. 75; 10 Comp. Cas. 173.

presented on behalf of the appellant on this aspect of the case consisted of an endeavour to draw a distinction between a lump sum paid at the beginning of the service and a sum paid, as in the present case, in consideration of an agreement to continue to serve for a reduced salary. There is no substance in this distinction. If a man who is serving at a salary of £1,000 a year agrees to serve for a reduced salary in consideration of a lump sum, he is merely commuting his salary, and a sum so accepted in commutation of salary can in its nature be nothing but salary. The commutation merely substitutes one form of remuneration for another. It is, in effect, remuneration payable in advance and it is quite fallacious to speak of it as a capital payment. Indeed, I am unable to understand how a sum paid as remuneration can ever be capital in the sense that it escapes taxation, since remuneration as such is the subject-matter of tax under Schedule E whatever form it takes. The analogy of cases such as the sale by an annuitant of his annuity for a lump sum is a false one since the quality of remuneration is absent from the payment.

The real difficulty in the case arises by the introduction into the agreement of the provisions relating to the pension. If the agreement had merely provided for the surrender of the pension in consideration of a present payment, with no reference to or connection with present or future services, I do not think that the sum received would have been taxable under Schedule E since it would not have been remuneration or salary for services. It would have been nothing more nor less than commutation of a pension, and a pension is in itself a distinct taxable subject-matter. It was admitted by the Attorney-General that a sum received in commutation of a pension effected after the termination of the service is not taxable. But he maintained that the case is different where the commutation takes place during the continuance of the service, and that a sum paid then must necessarily be regarded as remuneration for service rendered and to be rendered. I do not think that this view is correct. It would, of course, be possible for an employee to agree to give up his future pension rights in consideration of a present addition to his salary, and in that case the addition would be remuneration and taxable as such, notwithstanding that it originated in a surrender of pension rights. The question whether a sum received in consideration of the surrender of future pension rights is or is not remuneration must, as it appears to me, depend upon the true construction of the agreement by which the transaction is effected. If the sum received is by way of an addition to remuneration, in the form either of an increase in periodical salary or of a lump sum, it is taxable; if it is not so received, but is merely paid by way of commutation of a future pension without reference to

or connection with the service, it would not, I think, be taxable. The same result would, I think, have followed in the present case if the agreement had been framed in two distinct parts: one an agreement to serve at a reduced salary in consideration of £x, the other an agreement to give up the pension rights in consideration of £y. In that case the sum £y could not, as it appears to me, have been described as remuneration for services.

It was argued on behalf of the appellant that if the whole £40,000 does not escape taxation, it ought to be regarded as referable in part to the acceptance of a reduced salary and in part to a commutation of future pension rights and apportioned accordingly. I was impressed by this argument, but on consideration I am unable to accept it. The question, as I see it, turns upon the actual language of the agreement. The parties themselves have made no attempt to apportion the £40,000, no doubt because of the practical difficulty of doing so when the commencing date of the pension was unascertainable and an actuarial valuation accordingly impossible. Instead, they have chosen to treat the £40,000 as an indivisible sum paid "in consideration of the premises." The consideration is thus agreed to be an entire non-severable consideration, the whole of which is referable to the agreement to serve at a reduced salary just as much as to the agreement to give up the pension rights. It may well be that an apportionment might properly be made if, for example, a lumpsum were paid in consideration of an agreement to serve and of the sale of a piece of land by the employee to his employer. In such a case the land would be capable of valuation, and the parties must be presumed to have known it, and the agreement for sale would have no connection with the agreement to serve. But here one of the considerations for the entire sum is expressed to be the agreement to serve, and as the parties have so agreed I do not think that an apportionment is permissible, since it would involve rewriting the contract. It was argued by counsel for the appellant that the present case is covered by the decision in *Dewhurst v. Hunter*¹. I did not obtain any real assistance from the elaborate discussion of that decision which took place before us. It was a very special case and the contract did not contain peculiarities of the contract which are found in the present case, to which I have referred. As I have said, this case, in my opinion, falls to be decided on the terms of the bargain which the parties have themselves made, which is, in essential respects, different from that in *Dewhurst's Case*¹, and counsel's argument for the appellant that the facts of the present case are in all essentials indistinguishable from those in *Dewhurst's Case*¹ is one that I cannot accept. I would dismiss the appeal.

(1) (1932) 16 Tax Cas. 605.

MACKINNON, L. J.—Lawrence, J., has held that the appellant is liable to pay income tax under Schedule E of the Finance Act, 1918, upon the £ 20,000 paid to him by the company on April 6, 1938, and upon the £ 20,000 so paid on April 6, 1939. In other words, each of these sums was “an annuity, pension, or stipend.....in respect of salaries, fees, wages, perquisites, or profits.....for the year of assessment.” The special case sets out the agreements of December 19, 1921, and of March 31, 1937. I need only remark of the latter that it is obvious that the provision in it for the payment of £4,000 a year for ten years from the date of Mr. Tilley’s ceasing to be a director involves a nice question of construction, namely, what, if any, are the rights of his executors or administrators if he should die (a) while he is still managing director, or (b) after he has ceased to be managing director, but when only some of the annual sums of £4,000 have been paid? The 1938 agreement provided (1) that the company should be released from the obligation to pay the £ 4,000 a year, “pension” for ten years; (2) that Mr. Tilley should serve the company as managing director at a salary of £ 2,000 a year instead of £ 6,000; no period for such service is fixed, so presumably it would be for a reasonable time; and (3) that the company should pay him £ 20,000 on April 6, 1938, and £ 20,000 on April 6, 1939. The date “April 6” is perhaps not without significance in a case about income-tax.

The problem is whether these two sums of £ 20,000 are taxable in the two years of receipt under Schedule E. If I were not assisted, or embarrassed, by decisions of the House of Lords which are reported, I should think the answer was “Yes”, as was held by Lawrence, J. Each £20,000 must have been paid partly in consideration of Mr. Tilley accepting for the future £2,000 a year salary in place of the £ 6,000 a year he was entitled to under the 1937 agreement, and partly in consideration of his releasing the company from the obligation under that agreement to pay him £ 4,000 a year for ten years. As regards the first sort of consideration, if a servant were entitled to £ 10 a week, and on April 6 he agrees, in consideration of £ 520 paid down, to serve for a year for nothing, the £ 520 would pretty clearly be an annual receipt within Schedule E. So if a servant has an annual salary of £ 2,000 and in consideration of £ 20,000 paid down he agrees to serve for ten years for nothing. And if, as here, he is entitled to be paid £ 6,000 a year for an unspecified time, and in consideration of £x paid down he agrees to serve for a reasonable time for £2,000 a year instead of £6,000 a year, I should think the £x would be in the same position.

So far as each £20,000 was in consideration for the surrender or abolition of the right to the “pension” *in futuro*, the position may not

be so clear. No doubt, if a man had, under an endowment policy, a right to be paid £x a year by an insurance company and he sold or surrendered this right to the insurance company for a lump sum, that lump sum would not be taxable under Schedule E. But why would it not be so? Not, I think, from any characterisation of the sum as "capital" rather than "income", but because the annual sum he was to receive, and was surrendering, was not "an annuity, stipend, or pension in respect of salaries, fees, wages, or profits." That being so, the lump sum received by way of commutation could not be within that category. The question, as I see it, is whether the so-called "pension" is within that category, *i.e.*, payment by way of salary or wages for services rendered. If it is, then I should think the lump sum payable *in praesenti* for its satisfaction is also within that category. If the 1937 agreement had remained in force, and the ten sums of £4,000 had been paid, I should myself have thought that each of them, in its year of receipt, would be taxable under Schedule E as an "annuity, stipend, or pension, in respect of salaries, fees, wages, or profits." Each would be, in effect, deferred remuneration for services rendered in the past. And if that be so I should think that the lump sum agreed to be paid in advance in satisfaction or commutation of such deferred remuneration would also be within Schedule E.

This, as I have said, would be my view if there were no reported cases to assist, or perhaps embarrass, me. But there are two such cases, *Dewhurst v. Hunter*¹ and *Cameron v. Prendergast*². Both are decisions of the House of Lords. The former was decided by three votes to two; the latter was the unanimous decision of five noble Lords, of whom none were participants in the former. So far as the two sums of £20,000 were paid in consideration of Mr. Tilley agreeing to serve for £2,000 a year in place of £6,000 a year, the decision in *Cameron v. Prendergast*² seems clear authority that the amount so paid is taxable under Schedule E. It is to be observed that Cameron, like Tilley in this case, did not agree so to serve for any fixed period of time. But so far as the two sums of £20,000 in this case were paid in consideration of the surrender of the prospective right to the £4,000 a year pension, the decision in *Dewhurst's Case*¹ seems to me to make it very difficult, if not impossible, to hold that that part of the £20,000 is taxable under Schedule E, for I cannot think that there is any essential difference between the sum which Dewhurst would have been entitled to under article 109 and the sums which Tilley would have been entitled to under his 1937 agreement. Dewhurst would have got a lump sum and Tilley would have got ten annual payments. But I do not see how that

(3) (1932) 16 Tax Cas. 605.

(2) (1940) 8 I.T.R. Suppl. 75; 10 Comp. Cas. 173.

difference can alter the nature of their respective gains; and if a prepayment in satisfaction of Dewhurst's prospective right was not within Schedule E, I have great difficulty in seeing how the prepayment in satisfaction of Tilley's prospective right can be. If a single payment has been made for two sorts of consideration, one of which does make part of the sum taxable, while the other does not, the Commissioners would have to ascertain how much of the total sum fell within each category. Suppose, for example, a director received £10,000 from his company; it is found to have been paid under a resolution of the Board "that Mr. A be paid £10,000 in satisfaction of his claims (a) for his fees for last year as a director, and (b) in payment for his patent No. — which he has assigned to the company." Obviously the Commissioners would have to analyse the £10,000 and find how much was payable under (a) and therefore was taxable.

In these circumstances I should be inclined to think that this case must go back to the Commissioners for them to find how much of the two sums of £20,000 was paid in consideration of the reduction of his salary (with a direction that the sum so found is taxable under Schedule E) and how much was paid in consideration of the surrender of his right to the £4,000 a year "pension" (which sum would not be so taxable). I realise that this would be a difficult problem, by reason of (a) the doubtful effect in law of Mr. Tilley's death, which I mentioned above, and (b) that the agreement of 1938 fixes no period for his service at the reduced salary. But if the law requires the Commissioners to ascertain a fact I doubt if the difficulty of performing their task can relieve them of the duty. My own inclination, therefore, is to think that the case ought to be sent back to the Commissioners in this way. But I can pretend to no disappointment at finding that my brethren think this view is incorrect, and that this appeal should be dismissed, for that is the result I should certainly have arrived at upon my own view of the law if I were happily oblivious of the existence of *Dewhurst's Case*¹ and free from the constraint of attempting loyally to follow it.

GODDARD, L.J.—In my opinion, the question in this case depends for its solution on the true meaning and effect of the agreement of April 6, 1938. It has now been decided by the House of Lords in *Cameron v. Prendergast*² that if a lump sum is paid to a director to induce him to continue to serve the company, either for no salary or at a reduced rate of salary, that payment is a profit of his office and is taxable. It is as though, instead of agreeing to serve, say, for five years at £1,000 per annum, he agreed to serve for five years for one

(1) (1932) 16 Tax Cas. 605.

(2) (1940) 8 I.T.R. Suppl. 75; 10 Comp. Cas. 172.

payment of £ 5,000. If, however, a director is entitled to receive on the termination of his office a fixed sum or a pension, and he compromises that right by acceptance of a smaller sum, then *Dewhurst's Case*¹ decides that the sum he receives is not income, nor, according to the view expressed by Lord Atkin in that case, is it to be regarded as received under or from the contract of employment.

In the present case Mr. Tilley was, under the agreement of June 28, 1937, entitled to a total salary of £ 6,000 while he served as managing director, and to a pension of £ 4,000 for ten years payable from the date when he ceased to hold his office. The agreement contained no provision as to the period for which he was to serve as managing director; the appointment could be determined by either side at any time, though presumably only upon reasonable notice. By the 1938 agreement Mr. Tilley, in consideration of £ 40,000, to be paid in two instalments, released the company from its obligation to pay him a pension and agreed to serve the company from the date of the agreement at a reduced salary of £ 2,000. Again, no period was fixed during which he was to serve. In my opinion, had the agreement been one under which Mr. Tilley agreed to commute his pension for £ x and also to accept a reduced salary in consideration of a payment of a lump sum, on the authority of the cases above referred to the result would have been that the sum representing the commutation of the pension would not have attracted tax, while that which represented or was taken in lieu of the larger salary would have been taxable. But that is not, in my opinion, the true result of the agreement. The consideration is entire, and Mr. Tilley covenants to continue to serve the company for £ 40,000 plus two thousand a year, instead of £ 6,000 per annum plus the prospect of a pension. I am, therefore, unable to avoid the conclusion that the £ 40,000 was remuneration for serving as a director, and I do not see that remuneration can ever be capital. There was, as it seems to me, a very good reason why the sum was not allocated partly to the reduction in salary and partly to the commutation of pension. As no one could say when the pension would become payable, it would be impossible to calculate its present value, apart, moreover, from the question that might arise on the construction of the clause granting the pension, whether, for instance, it would enure to the benefit of Mr. Tilley's estate if he died before ten years had elapsed, or had died while he was still in office. There is one point, however, on which I am not sure that I fully understand the judgment of Lawrence, J. If he meant that whenever a pensioner commutes a pension the sum received by way of commutation

(1) (1932) 16 Tax Cas. 605.

is taxable as income, as at present advised I do not agree with him; nor am I able to see that it makes any difference whether the commutation takes place before or after the pension has become payable. Schedule E charges pensions and annuities as specific things, in addition to charging profits arising from office, and if a commuted pension or annuity were taxable as income in the year that the sum was received, I cannot understand why it should make any difference whether the calculation and payment take place while the pensioner is still in the service of the grantor or not. Nor does it seem to me to be right to say, as the Attorney General submitted, that a pension must be deferred remuneration. Whether it be paid as a matter of contract or voluntarily, it may be a reward for or an inducement to render long service. For instance, an employer may pay all his clerks of a certain grade £5 a week and be willing to pay no more. If he promises a pension of £2 a week after thirty years' service I do not see that this would be an inducement to them to remain in his employment, or, if paid voluntarily, a recognition of long and faithful service. I agree with the Master of the Rolls that the appeal should be dismissed.

Appeal dismissed.

Leave to appeal to House of Lords.

[IN THE COURT OF APPEAL].

HENRIKSEN (INSPECTOR OF TAXES)

v.

GRAFTON HOTEL, LTD.

LORD GREENE, M.R., DU PARCQ, L.J., SINGLETON, J.

April 23, 24, 25; May 13, 1942.

INCOME-TAX—BUSINESS EXPENDITURE—MONOPOLY VALUE PAID BY LESSEES—PAYMENTS NOT DEDUCTIBLE FOR INCOME-TAX PURPOSES—LICENSING (CONSOLIDATION) ACT, 1910 (10 EDW. 7 & 1 GEO. 5, C. 24), SECTION 14—INCOME TAX ACT, 1918 (8 & 9 GEO. 5, C. 40), SCHED. D.

Lessees of licensed premises, under a covenant in their lease, paid annually certain sums imposed by the licensing justices as instalments of the monopoly value on the grant and renewal of the licence for three-year periods. It was contended that those sums were not capital payments, but must be regarded as revenue payments and, as such, deductible for income-tax purposes:—Held, affirming the judgment of Lawrence, J., that monopoly value payments were imposed for the term of the licence on grant or renewal, though the fact that permission was given to pay by yearly instalments gave a false appearance of periodicity. Such

payments fell into the same class as a premium paid on the grant of a lease, which admittedly was not deductible for income-tax. Therefore the payment in the present case must be regarded in law as out of capital, not revenue, and the claim to deduct it for income-tax failed.

Decision of Lawrence J., [1942] (1 K.B. 82 ; 10 I.T.R. Suppl. 79) affirmed.

Cases referred to :—

Addie & Sons, Collieries, Ltd. v. Inland Revenue Commissioners (1924) 1924 S. C. 231 ; 8 Tax Cas. 671.

Appenrodt v. Central Middlesex Assessment Committee (1936) 105 L.J.K.B. 492 ; (1936) 2 K.B. 447 ; affirmed in C.A. (1937) 106 L.J. K.B. 690 ; (1937) 2 K.B. 48.

British Insulated and Helsby Cables, Ltd. v. Atherton (1925) 95 L.J.K.B. 336 ; (1926) A.C. 205 ; 10 Tax Cas. 155.

Inland Revenue Commissioners v. Adam (1928) 1928 S.C. 738 ; 14 Tax Cas. 34.

Inland Revenue Commissioners v. Truman, Hanbury, Buxton & Co. (1913) 82 L.J.K.B. 1042 ; (1913) A.C. 650.

Kneeshaw v. Abertolli (1940) 100 L.J.K.B. 760 ; (1940) 2 K.B. 295 ; 9 I.T.R. Suppl. 121.

R. v. Sunderland Customs and Excise Commissioners (1913) 83 L.J.K.B. 51 ; (1913) 3 K.B. 483 ; affirmed in C.A. (1914) 83 L.J.K.B. 555 ; (1914) 2 K.B. 390.

R. v. Taylor ; R. v. Amendt (No. 2) (1915) 84 L.J.K.B. 1489 ; (1915) 2 K.B. 593.

Usher's Wiltshire Brewery Co. v. Bruce (1914) 84 L.J.K.B. 417 ; (1915) A.C. 433 ; 6 Tax Cas. 399.

Appeal from the judgment of Lawrence, J.

The appellants, Grafton Hotel, Ltd., under a fourteen years' lease granted by Associated London Properties, Ltd., carried on business as licensed victuallers in London, under a justices' licence for the period from November 11, 1931, to July 5, 1934, and the sum of £825 was imposed as monopoly value, payable in three yearly instalments of £275 each on October 1 of the three years 1931, 1932 and 1933. When the licence was renewed for the period January 5, 1934 to 1937, the monopoly value was reduced to £570, payable as before in three yearly instalments of £190 each, and on further renewal for the period 1937—1940 the monopoly value was again fixed at £570, to be paid in three annual instalments. The payments required were made by the company. The appeal related to the last instalment under the second grant and the first instalment under the third grant.

It was submitted on behalf of the company that the payments were necessary expenses of carrying on the trade or business, and that the yearly profits of the trade or business could not be ascertained without deducting the payments ; further, that the payment made each year was not in the nature of a capital payment by the company, but was a payment which had to be made on the due date in order to enable the company to carry on or to continue the business. Such payments should be classed as revenue payments and therefore deductible for income-tax. On behalf of the Crown it was argued that the payment

of monopoly value was an essential preliminary to the carrying on of the trade of a licensed victualler, whether the payments were made in one sum or by instalments, and that the payments were of a capital nature. Consequently the company were not entitled to deduct for income-tax purposes sums paid by them in respect of monopoly value.

The Commissioners decided in favour of the company, but Lawrence, J., reversed that finding, holding that monopoly value payments were payments out of capital. The company appealed.

Tucker, K. C., and S. Pascoe Hayward, for the appellants.

The Attorney-General (Sir Donald Somervell, K.C.) and R.P. Hills, for the Crown.

May 13.—LORD GREENE, M. R., stated the facts and continued: The General Commissioners decided in favour of the appellants, but their decision was reversed by Lawrence, J., and this appeal results.

A new justices' on-licence granted under the Licensing (Consolidation) Act, 1910, Section 14, takes one of two forms. It may be an annual licence, or it may under sub-section (2) be a licence for a term not exceeding seven years. Paradoxically, the annual licence gives in practice a more secure tenure to the licence-holder. Where the licence is granted for a term, an application for a re-grant at the expiration of the term is treated as an application for the grant of a new licence, with all the difficulties which that involves. An annual licence, on the other hand, is in ordinary circumstances renewed every year as a matter of course. On the grant of a new on-licence the justices are bound to attach conditions "for securing to the public any monopoly value which is represented by the difference between the value which the premises will bear in the opinion of the justices, when licenced, and the value of the same premises if they were not licenced." These conditions must be imposed whichever of the two forms above mentioned the licence may take but in practice there is a difference in application, since in the case of the licence for a term it is only payment of the part or "slice" of the monopoly value which is referable to the term of the licence that is exacted. The advantage of this method of procedure is that the payments which the licensee is compelled to make for one period can be adjusted in a subsequent period so as to reflect what experience shows to be the real monopoly value. It will be seen, therefore, that in the present case the sums fixed by the Justices in the case of each of the three grants was intended to represent that part or "slice" of the monopoly value which was referable to the period covered by the licence. These sums were made payable by annual instalments but this circumstance clearly cannot affect the character which for

present purposes must be ascribed to the payments. If the sum payable is not in the nature of revenue expenditure, it cannot be made so by permitting it to be paid by annual instalments. These payments by instalments in respect of monopoly value have not the annual quality of the payments for the grant of the annual excise licence, but are of a different character altogether.

It was not seriously argued that the payments now in dispute fall within the list of prohibited deduction set out in Rule 3 of the Rules to Cases I and II of Schedule D. The question therefore is, to quote the language of Lord Sumner in *Usher's Wiltshire Brewery Co. v. Bruce*, is the deduction claimed "on the facts of the case a proper debit item to be charged against incomings of the trade when computing the balance of profits of it" (84 L.J.K.B., at p. 435; [1915] A.C., at p. 468). This, of course, is to state the problem, not to solve it, since it remains to discover whether the item is proper one to be charged. For this purpose the first thing to do is to examine the nature of the payment, that is to say, the nature of the subject in respect of which the payment is made. In this connection the manner of payment may be relevant as throwing light upon its nature. In many cases—and in my opinion this is one of them—the question will be found to answer itself once the true nature of the payment is ascertained. Here the appellants were minded to acquire as asset in the shape of a licence for a term of years. As a condition of obtaining it, payment had to be made of a sum sufficient to secure to the public that part or slice of the monopoly value which was referable to the period of the licence. The effect of the licensing law is, of course, to grant to a licensee what for practical purposes and in respect of a particular area is in truth a monopoly. What the grantee of a licence is under Section 14 compelled to do is, so to speak, to purchase the monopoly rights for a sum equal to their value. The public confers the monopoly upon him, he must pay the public its value, although in the case of a licence granted for a period under sub-section (2) he pays not for the whole monopoly value but only for a part of it.

The nature of the payment which justices are to fix in respect of monopoly has been considered in a number of cases. It is true that these cases were not concerned with questions arising under the Income Tax Acts. They do, however, show what the nature of the payment is as between the licensee and the public and as between a hypothetical tenant and his landlord. In other words they show what it is that the licensee is paying for. Thus, in *Inland Revenue Commissioners v. Truman, Hanbury, Buxton & Co.*, Lord Haldane, L.C., observed (82 L.J.K.B., at p. 1047; [1913] A.C., at p. 659) that the

corresponding section which he was there considering dealt "not with the annual value of the licence but with its capital value". In *R. v. Sunderland Customs and Excise Commissioners*¹, justices had omitted to estimate the monopoly value at a definite capital sum and had instead exacted payment of an annual sum representing a percentage of gross takings. This it was held they were not entitled to do. Lord Cozens-Hardy, M.R., said (83 L.J.K.B., at p. 577; [1914] 2 K.B., at p. 397): "This is a lump sum, to be ascertained once for all, though when so ascertained it is competent to the justices in their discretion to say how that monopoly value is to be secured to the public and whether it is to be paid in one sum or by instalments". Joyce, J., said (83 L.J.K.B., at p. 560; [1914] 2 K.B., at p. 403): "I have not succeeded in finding anything in the Act to countenance the view that there is any such thing as annual monopoly value." The last of these cases is a rating case in this Court—*Appenrodt v. Central Middlesex Assessment Committee*². There it was decided that in fixing the estimated rent which the hypothetical tenant would be expected to pay, the liability for instalments payable in respect of monopoly value ought not to be taken into account. It is not necessary to consider this decision in any detail. Lord Wright, M.R., (106 L.J.K.B., at p. 693; [1937] 2 K.B., at p. 54) approved the statement of Lush, J., in the Divisional Court in *R. v. Sunderland Customs and Excise Commissioners* (83 L.J.K.B., at p. 57; [1913] 3 K.B., at p. 497) that the sum fixed for monopoly value is "the capital sum which represents the monopoly value" which he said, is only repeating the clear words of Section 14 (1) "that the capital payment is based on the value of the premises and has directly nothing to do with annual value or with rent". He then went on to point out that in a case falling under sub-section (2) (as did the case before this Court) the payment "though it concerns the market value of the hereditament it is limited to the number of years (not exceeding seven) for which the new on-licence is granted; a further similar charge for a further period of monopoly value may be imposed, it seems, at the expiration of the term". Later he said (106 L.J.K.B., at p. 693; [1937] 2 K.B., at p. 56): "The justices' licence is essential to give the premises the status necessary to enable a licensed victualler's business to be carried on". Romer, L.J., said (106 L.J.K.B., at p. 693; [1937] 2 K.B., at p. 61): "The instalments are an expense necessary for the accrual to the hotel of the incorporeal condition of being licensed premises". It is true that Scott, L.J., thought (106 L.J.K.B., at p. 699; [1937] 2 K.B., at p. 69)

(1) (1914) 83 L.J.K.B. 555; (1914) 2 K.B. 390.

(2) (1937) 106 L.J.K.B. 690; (1937) 2 K.B. 48.

that a payment under sub-section (2) is not necessarily a true capital payment, and he referred to the possibility of a fixation of the annual value of the monopoly. With respect I doubt whether it is open to justices to do this. But in any case, Scott, L.J., clearly regarded payment in respect of a five and a quarter years' period (which was the case before him) as a capital nature since later in his judgment he treats the acquisition of the monopoly as being on the same footing as any capital improvement of the property effected before the licensed house was open for business, such as a swimming pool. It is to be noted that the provisions as to fixing monopoly value appear in sub-section (1), and there is nothing in the section to suggest that any change in the character of the payment or the method of fixing it takes place where a licence for a term is granted under sub-section (2). It is true that in the two earlier cases the observations which I have quoted were not directed to the case of a licence granted for a term, and it is argued that for income-tax purposes at any rate the payments in such a case fall into a different category. This argument cannot, in my opinion, be sustained. The fact that under sub-section (2) the licence is granted for a term and the payments are made in respect of the term gives a false appearance of periodicity to the payments. In the normal case the grantee of a new on-licence under sub-section (2) no doubt looks forward to a renewal of his licence and not unnaturally regards the payments which he makes as periodical payments. Indeed, he may well decide in his accounts to debit them to revenue account. This, however, is by no means conclusive as to their nature. Traders frequently prefer to debit to revenue account payments which are in their nature proper to be carried to capital account. If they do so, it means nothing more than that they have a conservative taste in the matter of accountancy.

It appears to me that there can be no difference in principle between a payment out-and-out for monopoly value and a payment in respect of a term. Each licence granted for a term must stand by itself, since an application for its renewal falls to be treated as an application for a new licence. This is what I mean when I say that there is a false appearance of periodicity about these payments. Whenever a licence is granted for a term, the payment is made as on a purchase of a monopoly for that term. When a licence is granted for a subsequent term, the monopoly value must be paid in respect of that term, and so on. The payments are recurrent if the licence is renewed; they are not periodical, so as to give them the quality of payments which ought to be debited to revenue account. The thing that is paid for is of a permanent quality, although its permanence, being conditioned by the

length of the term, is short-lived. A payment of this character appears to me to fall into the same class as the payment of a premium on the grant of a lease which is admittedly not deductible. In the case of such a premium it is nothing to the point to say that the parties, if they had chosen, might have suppressed the premium and made a corresponding increase in the rent. No doubt, they might have done so, but they did not, in fact, do so. The lessee purchases the term for the premium. There is no revenue quality in a payment made to acquire such an asset as a term of years. Another class of expenditure which is comparable to the payments now in question is expenditure on improvements to the property which justices may require to be made as a condition of granting a licence. Such expenditure would clearly not be deductible in so far as any rate as the work required went beyond mere repairs. If my view of the nature of this expenditure is correct, it is unnecessary to discuss the authorities in which questions relating to deductions have been considered, or to refer to the various attempts which have been made to find a formula for describing what is a proper item to be charged when computing profits in cases which do not fall within the list of prohibited deductions. I need only say that I have considered carefully the authorities to which we have been referred. They have been quoted again and again in the books and I do not propose again to quote them. But the conclusion to which I have come in the present case that the sums claimed are not deductible is, I think, entirely consonant with those authorities.

One other argument must be mentioned. It was said that whatever the position might be in the case where, for example, a freeholder obtains a licence and makes the necessary payments, there is a difference where the payments are made by a lessee under a covenant in that behalf contained in his lease. I do not follow this. If a payment is of such a nature as to preclude its deduction when made spontaneously, I cannot see that its nature is affected by reason of the fact that it is made under a covenant with a third party. Capital improvements are often made under a covenant in a lease. I have never heard it suggested that the cost of making them can be deducted by the lessee in computing his profits for income-tax purposes. An attempt was made to rescue this argument from shipwreck by saying that if the lessor had undertaken to bear these payments and had consequently exacted a higher rent, the full rent could have been deducted as an expense. This argument has a familiar ring. The answer to it is that this was not the contract which the parties chose to make. It frequently happens in income-tax cases that the same result in a business sense can be secured by two different legal transactions, one of which may

attract tax and the other not. This is no justification for saying that a taxpayer who has adopted the method which attracts tax is to be treated as though he had chosen the method which does not, or *vice versa*. The appeal fails and must be dismissed with costs.

DU PARCQ, L.J.—I agree that this appeal be dismissed.

[His Lordship set out the facts given above and continued:] The person liable to pay these sums of £ 570 under the justices' orders were, I think, clearly the licensees, though probably no one expected that the money would come out of their pockets. When it is desirable from the point of view of lessor and lessee alike that the demised premises should be licensed, it is necessary that they should agree how the cost is to be borne. The landlord may pay the cost and recoup himself by charging a higher rent. In the case of a short tenancy, for instance, that of the hypothetical tenant whose position had to be considered in *Appenrodt v. Central Middlesex Assessment Committee*¹, the landlord is very like to pay such a charge "just as much as that of any other element of value in the hereditament which he lets": (*per* Lord Wright, M.R., (106 L.J.K.B., at p. 694; [1937] 2 K.B., at p. 57) In the present case the lessees (the appellants) bound themselves to pay "all charges.....imposed" in respect of the licences. They accordingly came under an obligation to pay two charges, each of £ 570, in respect of the second and third licences. In 1934, and again in 1937, they were left, until a new licence was obtained, without the protection which would enable them to carry on their trade. The payment of the £ 570 was an expense which secured for them the right to open the Grafton Hotel as a licensed house: without that right they must either have ceased to trade there altogether, or carried on some different trade, but they could not have continued in business as licensed victuallers in those premises. In other words, when the licence dies, the trade dies, unless the grant of a new licence enables it to be carried on for a further period.

Thus the question which we have to consider comes to be whether a payment of a lump sum made to obtain permission to trade for a term of years is of such a character that it "is proper and necessary" to deduct it "in order to ascertain the balance of profits and gains": (see the speech of Lord Parker in *Usher's Wiltshire Brewery Co. v. Bruce* (84 L.J.K.B., at p. 429; [1915] A.C., at p. 458). It is conceded that if the payment was in the nature of a capital payment, it is not deductible. Unfortunately the expression "capital payment" does not appear to be capable of precise definition. At any rate I will not attempt to define it, but will confine myself to dealing with the facts of the present case. Here each sum in question was part of a total amount paid to acquire

the right to trade for a period of years. At the date when that period began, the possession of that right was essential before trading could be begun. In these circumstances, I am of opinion that each sum paid must be considered part of a capital outlay. This view is, I think, in accordance with the principle laid down by Viscount Cave, L.C., in *British Insulated and Helsby Cables, Ltd. v. Atherton*, when he said (95 L.J.K.B., at p. 340; [1926] A.C., at p. 218): "But when an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital. For this view there is already considerable authority."

In two Scottish cases, Lord Clyde (Lord President) formulated the question for decision as follows: "Are the sums in question part of the trader's working expenses, are they expenditure laid out as part of the process of profit-earning: or, on the other hand, are they capital outlays, are they expenditure necessary for the acquisition of property or rights of a permanent character the possession of which is a condition of carrying on the trade at all?": (see *Addie & Sons' Collieries, Ltd. v. Inland Revenue Commissioners* [1924] S.C., at p. 235), and *Inland Revenue Commissioners v. Adam* ([1928] S.C., at p. 742). It is true that the period for which the right was acquired in this case was three years and no more, and a doubt may be raised whether such a right is of "enduring benefit" or "of permanent character." These phrases, in my opinion, were introduced only for the purpose of making it clear that the "asset" or "right" acquired must have enough durability to justify its being treated as a capital asset. This is borne out, so far as Lord Clyde's judgments are concerned, by the fact that in *Adam's Case* the duration of the right acquired was eight years, and that his Lordship there spoke of its "relatively permanent character." "Permanent" is indeed a relative term, and is not synonymous with "everlasting." In my opinion the right to trade for three years as a licensed victualler must be regarded as attaining to the dignity of a capital asset, whereas the payment made for an excise licence is no doubt properly regarded as part of the working expenses for the year. For these reasons I have come to the conclusion that the Commissioners were wrong; not in their findings of fact, which are not disputed, but in the inference which they appear to have drawn from the facts, and that the decision of Lawrence, J., was right, and should be affirmed.

SINGLETON, J., after stating the facts, continued: It is to be remembered that under the Licensing (Consolidation) Act, 1910,

Section 14 (4), a new justices' on-licence granted for a term under the section may be forfeited if any condition imposed under the section is not complied with, by order of a Court of summary jurisdiction. Thus, failure to make any one of the payments might have resulted in loss of the licence, without which the business could not have been carried on. It becomes necessary, therefore, to consider what is the nature of the payment made as one of the conditions of the grant of a new justices' on-licence under Section 14 (1) (a) of the Act of 1910. The sub-section speaks of it as "any monopoly value which is represented by the difference between the value which the premises will bear, in the opinion of the justices, when licensed, and the value of the same premises if they were not licensed." This clearly indicates a capital value, an increased value attached to the premises. This was the view taken in *R. v. Sunderland Custom and Excise Commissioners*. Lord Cozens-Hardy, M.R., said (83 L.J.K.B., at p. 557; [1914] 2 K.B., at p. 397): "This is a lump sum, to be ascertained once for all, though when so ascertained it is competent to the justices in their discretion to say how that monopoly value is to be secured to the public, and whether it is to be paid in one sum or by instalments." Sir Samuel Evans, P., said (83 L.J.K.B., at p. 558; [1914] 2 K.B., at p. 399): "I think it is abundantly clear from the section that the 'monopoly value' must be a definite sum fixed once for all when the licence is applied for, and before it is granted. When it has been fixed, the justices must take measures by the conditions attached to the grant to secure it to the public; and they can include in the conditions provisions for payment by instalments; but by sub-clause (b) of sub-section (1) the amount of any payments imposed under the conditions shall not exceed 'the amount thus required to secure the monopoly value.' It follows that the monopoly value cannot be left to be ascertained or fixed either by the justices, or by anybody else, annually, or periodically." And Joyce, J., said (83 L.J.K.B., at p. 560; [1914] 2 K.B., at p. 408): "I have not succeeded in finding anything in the Act to countenance the view that there is any such thing as annual monopoly value. I think there is not." The same view was taken by Lawrence, J., in *Kneeshaw v. Abertollit*. It is unnecessary to express a view as to whether what he said as to the mode of assessing monopoly value in the case of a licence granted for a period of years is right or not, but it is clear that he was of opinion that the amount fixed by way of monopoly value was a capital sum.

In *Appenrodt v. Central Middlesex Assessment Committee*^a, the Court was dealing with a question under the Rating and Valuation

(1) (1940) 2 K.B. 295; 9 I.T.R. Suppl. 121.

(2) (1937) 106 L.J.K.B. 690; (1937) 2 K.B. 48.

Act, 1925, and the point which arose was whether instalment payments made by the owner occupier of licensed premises in respect of monopoly value of a licence granted for a period of five and a quarter years could be taken into consideration by way of diminishing the estimated rent which a hypothetical tenant would pay for the premises. The Divisional Court had held that the payments ought not to be taken into consideration, and from two of the judgments at least it is clear that the payments were to be regarded as payments of a capital nature. The Court of Appeal affirmed the decision of the Divisional Court on somewhat different grounds. Reliance was placed by counsel for the appellant on the judgment of Scott, L.J., in this case; on the other hand, the Attorney-General submitted that if it were carefully examined it was really support for the case of the Crown. Scott, L.J., said (106 L.J.K.B., at p. 698; [1937] 2 K.B., at p. 66): "The Divisional Court have, however, decided that the amount of rent which the hypothetical tenant would be willing to pay is not in law affected by the payments of monopoly value. The main reason for the decision, as explained by the Lord Chief Justice, was that a payment to be made for monopoly value is, according to the decision of the Divisional Court, affirmed by this Court, in *R. v. Sunderland Customs and Excise Commissioners*¹, and followed by Lord Reading in *R. v. Taylor, R. v. Amendt* (No. 2)², a capital payment, whether payable in one sum or in several instalments. The learned Chief Justice concluded his judgment thus (105 L.J.K.B., at p. 496; [1936] 2 K.B., at p. 455): 'But the one thing that is clear about it is that it is a part of capital value, and in those circumstances it seems to me that it is impossible to hold that the sum should be taken into account by way of deduction when the question is asked: What would the hypothetical tenant be prepared to pay by way of rent?' And I draw attention to another passage in the judgment of Scott, L.J., commencing at the words (106 L.J.K.B., at p. 699; [1937] 2 K.B., at p. 67): "I agree that instalments, etc.", and ending with the words: "As they have an unfettered discretion as to how they secure payment of the monopoly value during the period, I can see nothing to prevent their providing in each year for payment of an amount which they estimate will be the equivalent of the annual value of the monopoly in that year, if they so choose. But whether they make it a lump sum for the period payable once for all or by instalments, or an annual payment proper at the beginning of each year, seems to me immaterial. It shows, at any rate, that a payment under sub-section (2) is not necessarily a true capital payment."

(1) (1914) 83 L.J.K.B. 555; (1914) 2 K.B. 390.

(2) (1915) 84 L.J.K.B. 1489; (1915) 2 K.B. 593.

I confess that I find it difficult to reconcile some expressions of Scott, L. J., with the views of the Court of Appeal as expressed in *R. v. Sunderland Customs and Excise Commissioners*¹. If, as the Lord Justice said, the words "capital sum" were not used in the judgments in the 1914 case there were references to a "lump sum payment to be ascertained once and for all"; and Joyce, J., in his judgment made it clear that he could find nothing which pointed to an annual payment. And yet it must be borne in mind that in the 1914 case that which was being considered was a payment made for a licence granted under sub-section (1) of Section 14, while in *Appenrodt's Case*² it was a payment for a licence granted under sub-section (2). Scott, L. J., obviously thought that there might be a difference between the two, and that is something which has to be considered. In this connection it must not be over-looked that sub-section (1) alone deals with the payment which may have to be made, and it is not easy to see that a payment required under that sub-section may sometimes be a capital payment and at other times something quite different. Moreover, the monopoly value for which the payment is required attaches in a sense to the premises. The amount of it is determined in a normal case very much in the same way as compensation was determined in the case of a redundant old on-licence. That was always regarded as a capital sum, and so, I venture to think, has monopoly value been. I cannot help feeling that there has been some misunderstanding as to Section 14 of the Licensing (Consolidation) Act, 1910, which was in the same terms generally as Section 4 of the 1904 Act. I have always understood that the reason for sub-section (2) enabling a licence to be granted for a period was because of the difficulty of arriving at the amount to be paid by way of monopoly value. If the licensing justices granted the ordinary licence (spoken of as an annual licence) and fixed a sum to be paid for monopoly value, they could not afterwards alter that sum, however unfair it might turn out to be to the one side or to the other. And the difficulty in arriving at a figure in respect of a new house in a growing neighbourhood before trade has commenced is obvious. To avoid this difficulty, or to meet it to some extent, it was provided that a licence could be granted for a period, and when that course was adopted a more or less nominal payment was required in the first instance for monopoly value, and when the subsequent application was made the justices, with the help of the Commissioners of Customs and Excise and with knowledge of the trade of the house and of development of the neighbourhood, were in a much better

(1) (1914) 83 L.J.K.B. 555; (1914) 2 K.B. 390.

(2) (1937) 106 L.J.K.B. 690; (1937) 2 K.B. 48.

position to form a view as to what amount should be required by way of monopoly value. The first payment (already made) was regarded as in the nature of a payment on account, and a sum was fixed which was much more likely to be fair to both sides than one determined on the initial application could reasonably have been expected to be. (See note in *Paterson's Licensing Acts*, 51st ed., at p. 493.) If this be the correct view, a payment required on the grant of a licence under sub-section (2) is just as much a capital payment as it is in the case of a grant under sub-section (1), and that, I think, was the view of the Lord Chief Justice in *Appenrodt's Case*¹.

We were told by the Attorney-General that there was a practice in London of granting period licences again and again, as was done in the present case. Now it may be that that is strictly within the terms of sub-section (2) of Section 14, but I cannot think that it was the intention of the Legislature. If the justices adopt such a course, and if they time and again fix a sum for what is described as monopoly value for a period, they are, in my view, departing from the general understanding of monopoly value. The period may be a short one, and it can be argued that what they are then requiring from the applicant is a periodical payment to allow him to carry on his trade in that house. If that be the true position, they do not alter it by calling it a lump sum payable by instalments. In the case which we have to consider, on each of the last two applications the justices fixed the sum of £ 570, payable by instalments of £ 190 a year. It is at least akin to saying : " Pay £ 190 a year for the privilege of carrying on your trade on those premises." No doubt the justices had the help of the Customs and Excise (as representing the public) in arriving at the proper sum, and if they can be said to be parties to the fixing of a sum to be paid annually for these so called period licences the position is indeed confused. The case stated does not give the reasons for the decision of the Commissioners. If they had found as a fact that the justices had on either of the last two applications decided that £ 190 a year was the amount to be paid for the licence to trade during that year, it seems to me that it would have been difficult for any Court to interfere with their decision. In the absence of any such finding, we must come to the conclusion that the justices did that which was their duty and fixed a capital sum as the value of the monopoly. If that be so, the company is not entitled to have the amount of an instalment of a capital sum allowed as a deduction in calculating its yearly profits, any more than it would be if it had entered into a contract with the owners to rebuild or to make structural alterations (as distinct from repairs) which the licensing justices might require during the currency of the lease,

(1) (1937) 106 L.J.K.B. 690 ; (1937) 2 K.B. 48.

I have dealt with the Licensing Act, 1910, Section 14, at some length, because of what we were told as to the practice of granting period licence, not merely on the first application for a new justices' on-licence, but on subsequent applications. If this is done, and if a sum is required to be paid by way of monopoly value for a short period, it is arguable that the sum "is not necessarily a true capital payment," as Scott, L.J., said in *Appenrodt's Case*¹, but that it is rather an amount required for the privilege of carrying on the trade for the period. It may be that this was the view of the Commissioners, but they have not so found. In the course of the argument it was suggested that it might be necessary to send the case back for findings of fact, but counsel for the company said he could not ask the Commissioners to find that the justices had done something illegal, *id est*, that they had fixed a yearly sum instead of a capital sum. In the absence of any such finding by the Commissioners, I do not see that it is open to this Court to say that the sum fixed is other than a capital sum, and consequently I agree that the appeal fails.

Appeal dismissed.

Leave to appeal to the House of Lords.

[IN THE HOUSE OF LORDS.]

BEAK (INSPECTOR OF TAXES) v. ROBSON.

VISCOUNT SIMON, L. C., LORD ATKIN, LORD THANKERTON,
LORD RUSSELL OF KILLOWEN, LORD PORTER.

December 15, 1942.

INCOME-TAX—COMPANY—DIRECTOR—PAYMENT TO DIRECTOR FOR
NOT COMPETING AFTER TERMINATION OF SERVICE—WHETHER PROFIT
OF OFFICE—LIABILITY TO INCOME-TAX.

The assessee entered into an agreement with a company whereby he was to be employed for a term of five years as director and manager at a certain salary. Under the agreement the contract was made terminable by either side on six months' notice in writing. In the event of the assessee determining the agreement by notice or committing a breach of it which led to a determination, he covenanted for a stated period not to be engaged or interested in a competing business within fifty miles of Newcastle-upon-Tyne without the consent of the company. In consideration of his entering into that covenant the assessee was paid a sum of £ 7,000 which was assessed to income-tax as remuneration from the office of director or manager:

(1) (1937) 106 L.J.K.B. 690; (1937) 2 K.B. 48.

Held, (affirming the decision of the Court of Appeal) that the sum of £ 7,000 was not chargeable to income-tax under Schedule E, inasmuch as it was not a profit from the office of director and manager but was a payment made to the assessee under a separate covenant which came into effect only when the service was concluded.

By an agreement dated October 4, 1937, the assessee (Mr. Robson) agreed to serve a company as manager and director for five years at a salary of £ 2,000 per annum. The agreement was to be terminable by either party by six months' notice in writing expiring on September 30, 1940, or at any time thereafter. Clauses 7 and 8 were in the following terms:

"(7) In consideration of the restrictive covenant on the part of Mr. Robson contained in the next succeeding clause hereof the company shall on the execution hereof pay to Mr. Robson the sum of £ 7,000."

"(8) If this agreement shall be determined by notice given by Mr. Robson to the company under clause 6 hereof or by any breach by him of the provisions of this agreement, then from such determination or breach until the determination of a period of five years from April 1, 1937, Mr. Robson shall not without the consent in writing of the company either solely or jointly with or as manager or agent for any other person, persons or company directly or indirectly carry on or be engaged, concerned or interested in the business of coal exporter, coal merchant or shipbroker within fifty miles of Newcastle-upon-Tyne."

The sum of £ 7,000 was paid on the execution of the agreement and an assessment was made in this sum for the year ending April 5, 1939, under Schedule E of the Income Tax Act, 1918. Lawrence, J., cancelled the assessment and the Court of Appeal affirmed the decision of Lawrence, J.

The judgment of the Court of Appeal was as follows:—

LORD GREENE, M.R.—In my opinion this is a clear case and the decision of Lawrence, J., was manifestly right.

It is to be observed that the way in which the parties have chosen to contract is one in which the obligations flowing from the contract of service and the remuneration to be received by the respondent in respect of that service are entirely separated from the restrictive covenant and the consideration which is given for it. Separate considerations are fixed for the two things; one consideration for the service, a totally different consideration for the covenant. Breach of the contract of service has nothing to do with breach of the covenant. Conversely, breach of the covenant would have nothing to do with the contract of service.

It seems to me that those facts would by themselves be quite sufficient to dispose of this case. The sum of £7,000 is not paid to the respondent for performing the services in respect of which he is chargeable under Schedule E. The consideration which he has to give under the covenant falls to be given not during the period of his employment, but after its termination. In fact, he is selling to the company for a sum of £7,000 the benefit of a covenant which will only come into effect when the service is concluded. It seems to me that to say that that £7,000 is a profit or remuneration from his office is to ignore the real nature of the transaction.

But it is said that this covenant is a condition of the service into which he enters by agreeing to serve as director and manager. That observation is no doubt true, in the sense that this particular provision with regard to the covenant is found in the contract of service and no doubt the parties would not have entered into that contract of service unless that term had been agreed upon; but it seems to me impossible to proceed from that to the further step and say that because this provision is a condition of the service in that sense, therefore the remuneration paid is remuneration from the service. I put the example in the course of the argument of a man appointed a manager for a period of years at a definite remuneration. One of the terms might be that while the employment continues he is to use his motor car for the purposes of his employers. The contract might go on to say that on the termination of the employment he, in consideration of a sum paid down, would transfer the motor car to the employers as their own property. It seems to me it would be impossible to suggest in such a case that the sum he received in consideration for the undertaking to transfer the motor car would be remuneration from his employment. I cannot myself see any difference between that case and the present. In each case the employee is contracting to sell something to his employer at the termination of his agreement and receives a particular and specific consideration for it.

It was suggested then that restrictive covenants of this kind are commonly found in managerial agreements without there being any specific consideration allocated to them. That no doubt is true and in some cases covenants of that kind may be valid in law; but, quite apart from the question of their validity, it is common knowledge that many managerial agreements do contain clauses of that kind. If, for a fixed remuneration, a man agrees to serve and without any additional remuneration agrees to enter into such a covenant, I cannot myself see how it can be suggested that the covenant in some way or another must be regarded as something outside the contract of service.

It was suggested that if the respondent was successful in the present case it would be necessary—or legitimate at any rate—in all such cases as those to which I have referred to segregate the covenant not to compete from the covenants relating to the service and attribute some apportioned part of the consideration to the former, with the result that parts of salaries would escape taxation under Schedule E. Arguments of that kind can be dealt with if and when anyone has the hardihood to make such a claim; but that is not the present case. The fact that the parties could, if they had so desired, have cast their agreement in a form under which for increased remuneration the respondent agreed to serve and then merely gave this covenant, is beside the point. They have not done that. They have entered into an agreement which, although contained in one document and although made on the same occasion and although connected in the way I have indicated, really relates to two quite different matters, one the period of service, one something that is to happen after the service. The fact that they have decided on and allocated to that covenant an agreed consideration seems to me to take it right outside the class of case which I have just mentioned.

That really is enough to dispose of the case. In my opinion, the appeal fails and should be dismissed with costs.

DU PARCQ, L. J.—I agree.

LEWIS, J.—I agree.

The Crown appealed to the House of Lords.

Attorney-General (Sir Donald B. Somervell, K. C.) and Reginald P. Hills, for the appellant.

Cyril King, K. C., and John Charlesworth, for the respondent.

VISCOUNT SIMON, L.C.—My Lords, in this case the Crown contends that a payment of £ 7,000 to the respondent by a private company named William Mathwin & Son (Newcastle), Ltd., under a written agreement between them, dated October 4, 1937, was a “profit from the office” of director and manager of that company within the meaning of the Income Tax Act, 1918, Schedule E, Rule 1. The Commissioners for the General Purposes of the Income Tax Acts for the division of the City of Newcastle decided against this contention and were required to state a case for the opinion of the High Court. Lawrence, J., upheld the decision of the General Commissioners, and the Crown’s appeal to the Court of Appeal (Lord Greene, M. R., du Parcq, L. J., and Lewis, J.), failed. Leave was given to the Attorney-General to appeal to this House, on his undertaking that the Crown would pay the solicitor and client costs of the respondent in any event, and that the order as to

costs in the Court of Appeal would not be disturbed. Notwithstanding the able arguments addressed to us by the Attorney-General and by Mr. Hills, I am of the opinion that the decision appealed against is right and that the present appeal must be dismissed.

The written agreement of October 4, 1937, recites that Robson has for some years served the Company as a director and manager at a fixed salary with bonuses, and that his service is terminable by short notice on either side, but that his services and connection are important to the goodwill of the business. The provisions of the agreement are then set out in eight numbered clauses. Clauses 1-6 deal with the terms of Robson's service as a director and manager of the Company. He is to serve for a term of 5 years from April 1, 1937, at a salary at the rate of not less than £2,000 per annum, subject to a right in either party by 6 months' notice in writing to terminate the agreement not earlier than September 30, 1940. Provision is also made for the granting of bonuses to Robson out of the Company's profits, and during his service he is not to enter into any other business of a similar nature without the previous consent of the board. So far the clauses of the contract constitute a service agreement pure and simple.

Clauses 7 and 8 of the agreement deal with a different matter. Clause 8 binds Robson if his service in the Company is terminated before April 1, 1942, not to be concerned or interested in the business of coal exporter, coal merchant, or shipbroker within 50 miles of Newcastle-upon-Tyne until April 1, 1942, is reached. Clause 7 provides that in consideration of this restrictive covenant the Company shall on the execution of the agreement of October 4, 1937, pay to Robson the sum of £7,000. This sum has been duly paid and, as I have said, the Crown claims that it constitutes profit from Robson's office of director and manager and is taxable accordingly under Schedule E. Lord Greene, M.R., has indicated the answer to this claim in very clear language. In the agreement before us, the obligations flowing from the contract of service and the remuneration to be received by the respondent in respect of that service are entirely separate from the restrictive covenant and the consideration which is given for it. The sum of £7,000 is not paid for anything done in performing the services in respect of which Robson is chargeable under Schedule E. The consideration which he has to give under the covenant is to be given not during the period of his employment, but after its termination. He is giving to the company for a sum of £7,000 the benefit of a covenant which will only come into effect when the service is concluded. I agree with the Court of Appeal in the view that to treat this £7,000 as a profit arising from the respondent's office is to ignore the

real nature of the transaction. It is quite true that, if he had not entered into the agreement to serve as a director and manager, he would not have received £ 7,000. But that is not the same thing as saying that the £ 7,000 is profit from his office of director so as to attract tax under Schedule E.

The Attorney-General points out that it is not uncommon in managerial agreements to include a covenant not to compete after the service is terminated without any separate consideration being allocated to the covenant, and it was suggested that a decision in favour of the respondent in this case might involve the apportionment of the remuneration which a manager receives under his agreement between the profit of his office and the price paid to secure the covenant. I propose to say nothing about that, and to decide the present case purely upon the terms of the agreement of October 4, 1937. That agreement is admitted to be a *bona fide* contract and, so regarded, £ 7,000 cannot properly be treated as a profit arising from the respondent's office or employment.

I move that the appeal be dismissed with costs to the respondent as between solicitor and client.

LORD ATKIN.—My Lords, I agree.

LORD THANKERTON.—My Lords, I agree.

LORD RUSSELL OF KILLOWEN.—My Lords, I also agree.

LORD PORTER.—My Lords, I agree also.

Appeal dismissed.

[IN THE HOUSE OF LORDS.]

BRITISH-AMERICAN TOBACCO CO.

v.

INLAND REVENUE COMMISSIONERS.*

THE LORD CHANCELLOR (VISCOUNT SIMON), LORD ATKIN, LORD
THANKERTON, LORD RUSSELL OF KILLOWEN, LORD PORTER.

December 7, 8, 9, 1942.

COMPANY—'CONTROLLING INTEREST'—PROPRIETARY INTEREST NOT
ESSENTIAL—NO DISTINCTION BETWEEN DIRECT AND INDIRECT INTEREST—
FINANCE ACT, 1937 (1 EDW. 8 & 1 GEO. 6, c. 54), SCHED. IV, PARAS.
4, 7 (b), 11.

Schedule IV, paragraph 7 (b), of the Finance Act, 1937, provides that, for the purpose of the assessment of the amount payable out of trade profits in respect of National Defence Contribution "in the case of any other trade or business, being a trade or business carried on by a body corporate, the profits shall include all income received by way of dividend or distribution of profits from any other body corporate in which the first mentioned body corporate has a controlling interest and which is not liable to be assessed to the National Defence Contributions." By paragraph 4: "...where the trade or business is carried on by a company the directors whereof have a controlling interest therein, the directors shall be deemed to be carrying on the trade or business." By paragraph 11 the deduction to be allowed in respect of the remuneration of certain directors is limited where they have a "controlling interest":—Held, that the phrase "controlling interest" used in the above paragraphs does not necessarily connote a proprietary right, that is to say an interest in the nature of ownership, but covers the relationship of one company to another, where the requisite majority of one company's shares are, as regards their voting power, subject, whether directly or indirectly, to the will and ordering of the other company. A bare majority may be the requisite proportion of voting power.

Interpretation of "controlling interest" adopted by Rowlatt, J., in NOBLE v. INLAND REVENUE COMMISSIONERS [1927] (12 Tax Cas., at p. 926) approved.

Decision of the COURT OF APPEAL (111 L.J.K.B. 1; [1941] 2 K.B. 270; 10 I.T.R. Suppl. 67; 12 Comp. Cas. 129) affirmed.

* The phrase "controlling interest" occurs in Section 2 (21) and R. 7 (3) of Schedule I of the Excess Profits Tax Act, 1940, and the principles involved in this case are equally applicable to cases arising under the Excess Profits Tax Act.

Case referred to :—

Noble v. Inland Revenue Commissioners (1927) 12 Tax Cas. 911.

Appeal from the judgment of the Court of Appeal.

The facts are set out fully in 111 L.J.K.B., at p. 2; [1941] 2 K.B., at pp. 270, 271; 10 I.T.R. Suppl., at p. 68; 12 Comp. Cas., at p. 130.

Tucker, K. C. and *Scrimgeour*, for the appellant company.

The Attorney-General (*Sir Donald Somervell, K. C.*), *J. H. Stamp*, and *Reginald P. Hills*, for the Crown.

THE LORD CHANCELLOR (VISCOUNT SIMON).—This appeal is brought, by special leave of this House, from the order of the Court of Appeal (*Scott, L.J.*, *Clauston, L.J.*, and *Goddard, L.J.*) which dismissed an appeal by the appellants from a judgment of *Lawrence, J.*, on a case stated by the Commissioners for Special Purposes of the Income Tax Acts. The matter arises upon an assessment to National Defence Contribution made upon the appellant company under Part III of the Finance Act, 1937 and the question in dispute is whether the appellant company had “a controlling interest” in certain foreign companies referred to in the case within the meaning of that expression as contained in sub-paragraph (b) of paragraph 7 of the Fourth Schedule to the Act, so as to require that dividends received by the appellant company from these foreign companies should be included in its income liable to National Defence Contribution.

Counsel for the appellant company put forward two contentions in support of the view that the appellant company had no such controlling interest. First, he argued that “interest” in this connection means interest of a proprietary nature, and that the condition that there should be a controlling interest would only be satisfied if the appellant company itself owned sufficient shareholding in the other company to control the latter. Secondly, he contended that, in any event, a controlling interest is not constituted by the control of the bare majority of shares (whether directly or through other companies), but that the control must be of such proportion of shares as would secure the passing of a special resolution or other resolution for which a special majority is required by the terms of the constitution of the foreign company. These two contentions have been rejected as unsound by each tribunal which in turn has dealt with the appellant company's claim, and at each stage the decision arrived at has been in favour of the Crown. Notwithstanding the full and careful argument addressed to the House, I take the view that the decision arrived at below was correct, and I understand that your Lordships are in agreement with me that the appeal should be dismissed.

The case turns on the meaning of the words "controlling interest" in the context in which they are used. The appellant argues that in order that one company should have a controlling interest in another it must be the beneficial owner of a requisite number of shares in that other company, either registered in its own name or in the name of its nominees; and that if company No. 1 owns all the shares in company No. 2, which in turn owns all the shares in company No. 3, company No. 1 has no interest, controlling or otherwise, in company No. 3. It is true that in such circumstances company No. 1 owns none of the assets of company No. 2 and *a fortiori* owns none of the assets of company No. 3, and in that sense neither owns, nor has an interest in, company No. 3. But that is to treat the phrase "controlling interest" as capable of connoting only a proprietary right, that is, an interest in the nature of ownership. The word "interest", however, as pointed out by Lawrence, J., is a word of wide connotation, and I think the conception of "controlling interest" may well cover the relationship of one company towards another, the requisite majority of whose shares are, as regards their voting power, subject, whether directly or indirectly, to the will and ordering of the first-mentioned company. If, for example, the appellant company owns one-third of the shares in company X, and the remaining two-thirds are owned by company Y, the appellant company will none the less have a controlling interest in company X, if it owns enough shares in company Y to control the latter.

In my opinion this is the meaning of the word "interest" in the enactment under consideration, and where one company stands in such a relationship to another, the former can properly be said to have a controlling interest in the latter. This view appears to me to agree with the object of the enactment as it appears on the face of the Act. I find it impossible to adopt the view that a person who (by having the requisite voting power in a company subject to his will and ordering) can make the ultimate decision as to where and how the business of the company shall be carried on, and who thus has in fact control of the company's affairs, is a person of whom it can be said that he has not in this connection got a controlling interest in the company. As to what may be the requisite proportion of voting power, I think a bare majority is sufficient. The appellant company has, in respect of each of the foreign companies referred to in the case, the control of the majority vote. I agree with the interpretation of "controlling interest" adopted by Rowlatt, J., in *Noble v. Inland Revenue Commissioners* (12 Tax Cas. at p. 926), when construing that phrase in Section 53 (2) (c) of the Finance Act, 1920. He said that the phrase had a

well-known meaning and referred to the situation of a man "whose shareholding in the company is such that he is more powerful than all the other shareholders put together in general meeting". So here. The owners of the majority of the voting power in a company are the persons who are in effective control of its affairs and fortunes. It is true that for some purposes a 75 per cent. majority vote may be required, as, for instance (under some company regulations) for the removal of directors who oppose the wishes of the majority; but the bare majority can always refuse to re-elect and so in the long run get rid of a recalcitrant board. Nor can the articles of association be altered in order to defeat the wishes of the majority, for a bare majority can always prevent the passing of the necessary resolution. We are proceeding, in the absence of evidence as to foreign law, on the basis that the law governing these foreign companies does not differ materially from our own.

I move that the appeal be dismissed with costs.

LORD ATKIN.—My Lords, I agree.

LORD THANKERTON.—My Lords, I am of the same opinion.

LORD RUSSELL OF KILLOWEN.—My Lords, I also agree.

LORD PORTER.—My Lords, I concur.

Appeal dismissed.

[KING'S BENCH DIVISION.]

POPE (INSPECTOR OF TAXES) v. BEAUMONT.

MACNAGHTEN, J.

* July 18, 14, 1941.

INCOME-TAX—DIVIDEND PAID BY CO-OPERATIVE SOCIETY—SUM RETURNED TO TRADER MEMBER IN RESPECT OF WHOLESALE PURCHASES FROM SOCIETY—WHETHER CHARGEABLE WITH TAX AS DISCOUNT OR REBATE—INCOME TAX ACT, 1918 (8 & 9 GEO. 5, C. 40), SCHED. D, CASE I—FINANCE ACT, 1933 (23 & 24 GEO. 5, C. 19), SEC. 31.

The proprietor of a restaurant bought the meat required for his business wholesale from the co-operative society of which he was a member. The society were permitted by their rules to apply the net profits of all the business carried on by them to, inter alia, "a division, or return, to or among members.....in proportion to the amount of their purchases....." No discount was allowed to the proprietor at the time when he bought the meat, the whole price of which was accordingly debited in his profit-and-loss account. Having received £51 under the

society's rules in respect of his purchases of meat from the society during the relevant trading period, he was assessed to income tax in respect of that sum. He contended, however, that the sum was a dividend, exempt from tax under Section 31 of the Finance Act, 1938 :—Held that the sum so received was a rebate or discount, and so chargeable with tax; for, while rightly regarded by the society as a dividend, it was a return to the restaurant proprietor of part of the price paid for his meat.

Case stated by the Commissioners for the Special Purposes of the Income Tax Acts.

The respondent, F. W. Beaumont, a restaurant proprietor carrying on business at Stockton-on-Tees, bought ninety per cent. of the meat required for his business from the co-operative society of which he was a member. By rule 24 of the society's rules the net profits of all business carried on by the society was applicable "(d) to a division, or return, to or among members of the society in proportion to the amount of their purchases during the period to which the division relates." The dividend payable to a member was to be calculated by reference to his transactions with all departments of the society. In the material year of assessment the respondent received a dividend of £ 51 in respect of the £ 591 which he had spent in purchasing meat for the purposes of his business. No discount having been allowed to the respondent at the time of his various purchases, the full amount paid for meat was charged in his accounts. The £ 51 having been included as a receipt for the purposes of the respondent's assessment to income-tax under Case I of Schedule D to the Income Tax Act, 1918, for the material year, he appealed to the Special Commissioners.

On that appeal it was contended for the respondent that the £ 51 represented a dividend from the society which was exempt from income tax under Section 31 (3) of the Finance Act, 1938; that the dividend was not a rebate or discount on purchases; that as the society paid no separate dividend in respect of their butchering department, alone, the amount received by him as dividend was not a simple discount depending solely on, and proportionate to, his purchases when they were made, but depended on a number of factors relating to the society's trading as a whole; and that the £ 51 was therefore not a discount, but a dividend arising from mutual trading and, as such, a profit exempt from taxation.

It was contended for the Crown that the respondent used the society as wholesale suppliers, and that the £ 51 was a receipt of his trade to be brought into account as such for the purpose of his assessment to income tax.

The Commissioners held that that sum was not in the nature of a rebate or discount referable to the respondent's purchases of meat, but a dividend payable to the society's members in respect of their trading with all the society's departments, and reduced the assessment accordingly.

The Crown appealed.

The Attorney-General (Sir Donald Somervell, K.C.) and R.P. Hills, for the Crown.

F. Grant (for J. Alan Bell, on war service), for the respondent.

MACNAGHTEN, J.—Section 81 of the Finance Act, 1938, provides, so far as material, as follows: "In the application to any company or society of any provision . . . relating to profits or gains chargeable under Case I of Schedule D . . . any reference to profits or gains shall be deemed to include a reference to a profit or surplus arising from transactions of the company or society with its members which would be included in profits or gains for the purposes of that provision . . . if those transactions were transactions with non-members, and the profit . . . shall be determined for the purposes of that provision . . . on the same principles as those on which profits or gains arising from transactions with non-members would be so determined. . . . (3) . . . in computing, for the purposes of any provision . . . mentioned in sub-section (1) of this section, any profits or gains of a company or society which include any income which is chargeable to tax by virtue of the foregoing provisions of this section, there are to be deducted as expenses any sums which—(a) represent a discount, rebate, dividend, or bonus granted by the company or society to members or other persons in respect of amounts paid or payable by or to them on account of their transactions with the company or society, being transactions which are taken into account in the said computation: and (b) are calculated by reference to the said amounts or to the magnitude of the said transactions and not by reference to the amount of any share or interest in the capital of the company or society." In consequence of sub-section (3), the £51, although part of the net profits of the society's business, was nevertheless exempted in the calculation of the society's profits, as were also all sums paid to other persons under rule 24 (d) of the society's rules.

The question is whether this £51 was a rebate or discount. It seems to me plain that it was. It is described in rule 24 as "a division, or return, to or among members of the society." The words "division" and "return" are both, it would seem, appropriate to describe it. Considered from the point of view of the society, it was a dividend: it

was part of a sum which the society were dividing. Considered from the point of view of the purchaser of the meat, it was a "return" to him of part of the price which he had paid. True, it was not a return to which he was entitled as of right: whether or not he received it depended entirely on the society's decision to apply part of their profits in making such a return. When, however, the society decided to make out of their profits a return to customers, whether or not members, the sum returned appeared clearly as a rebate or discount on the price which the customers had paid. In my opinion the appeal should be allowed.

Appeal allowed.

[IN THE HOUSE OF LORDS.]

MCMILLAN v. GUEST.

LORD ATKIN, LORD WRIGHT, LORD ROCHE, LORD PORTER.

February 16, 17, 19, 28; April 27, 1942.

INCOME-TAX—DIRECTOR'S REMUNERATION—COMPANY—DIRECTOR RESIDING IN UNITED STATES PERFORMING WORK TO FURTHER COMPANY'S INTERESTS ABROAD—LIABILITY TO PAY INCOME-TAX ON REMUNERATION—INCOME-TAX ACT, 1918 (8 & 9 GEO. 5, c. 40), SCHED. E, R. 6.

A director of a private limited company incorporated under the Companies Acts in England whose seat of government was in England resided in the United States, performing work to further the interests of the company in that country, and during the whole period while so engaged, he did not attend any board meeting in England except one in 1931, and only one in Chicago in 1925. He was not required to attend board meetings and notices of such meetings were not sent to him.

Held, that the director held a "public office within the United Kingdom" and he was therefore liable to be charged to income-tax in respect of the profits of his office under Schedule E to the Income-tax Act, 1918.

Decision of the Court of Appeal [1941] (9 I.T.R. Suppl. 62) affirmed.

Cases referred to:—

Attorney-General v. Lancashire and Yorkshire Railway Co. (1864) 2 H. & C. 792; 33 L.J. Ex. 163; 10 L.T. 95.

Berry v. Farrow (1914) 1 K.B. 632; 83 L.J.K.B. 487; 110 L.T. 104.

Great Western Railway Co. v. Bater (1922) 2 A.C. 1; 91 L.J.K.B. 472; 127 L.T. 170; 8 Tax Cas. 231; (1920) 3 K.B. 266; (1921) 2 K.B. 128.

Pickles v. Foster (1913) 1 K.B. 174; 82 L.J.K.B. 121; 108 L.T. 106; 6 Tax Cas. 131.

Proctor v. Ryall (1928) 14 Tax Cas. 204.

Robinson v. Corry; Corry v. Robinson (1934) 1 K.B. 240; 103 L.J.K.B. 228; 150 L.T. 250; 18 Tax Cas. 411.

Watson v. Rowles (1926) 95 L.J.K.B. 959; 135 L.T. 614; 11 Tax Cas. 171.

Appeal from the Court of Appeal.

The facts are fully stated in the judgment of Lord Porter.

J. Millard Tucker, K. C., and *T. N. Donovan*, for the appellant.

The Attorney-General (Sir Donald Somervell, K. C.) and Reginald P. Hills for the respondent.

LORD ATKIN.—My Lords, this is an appeal from an order of the Court of Appeal reversing a decision of Lawrence, J., who allowed an appeal by the appellant, McMillan, from a determination of Commissioners for General Purposes of Income-tax upholding an assessment of the appellant for income-tax under Schedule E. The sole question is whether the appellant, who in the years of assessment was a director of a limited company, A. Wander, Ltd., had held a public office of profit within the United Kingdom. The facts are not in dispute, and are set out in paras 4-6 of the case stated by the General Commissioners, which I will not here repeat. The Income-tax Act, 1918, Schedule E, provides :

“Tax under Schedule E shall be charged in respect of every public office or employment of profit.”

By Rule 6 : “The tax shall be paid in respect of all the public offices and employments of profit within the United Kingdom.....*vis.*,(h) offices or employments of profit under any company or society, whether corporate or not corporate.....”

It is necessary to consider whether the appellant (1) held an office ; (2) held a public office ; (3) held a public office within the United Kingdom.

On the first point there was no dispute. There is no statutory definition of office. Without adopting the sentence as a complete definition one may treat the following expression of Rowlatt, J., in *Great Western Ry. Co. v. Bater*¹ as a generally sufficient statement of the meaning of the word :

“.....an office or employment which was a subsisting, permanent, substantive position, which had an existence independent of the person who filled it and which went on and was filled in succession by successive holders.....”

This statement was adopted by Lord Atkinson in his judgment in the same case in the House of Lords.² There can be no doubt that the director of a company holds such an office as is described.

It was contended by the appellant that, while he held an office, yet it was not a public office within the meaning of the Income-tax Act, 1918. It can hardly be said to be obvious that the position of director

(1) (1920) 3 K.B. 266 at p. 274.

(2) (1922) 2 A.C. 1 at p. 15.

of a trading company which may carry on business with a very small capital on a very small scale is necessarily a public office. It is, however, impossible to give effect to the words of Rule 6 (h) "any company" so as to distinguish between those whose offices are public and those whose offices are not. In particular, in reference to companies incorporated under the Companies Act it has to be remembered that the legislature has thought fit to impose duties upon their officers which attach to them as such and which are not imposed upon private partnerships, as for instance, Section 27, sub-section 2; Sections 37, 112, 122, 217 of the Companies Act, 1929. I can find no reason for distinguishing in this respect between offices held in a private company within the meaning of the Companies Acts (which this is) and a public company. Some of the above sections, though not all, apply to both. The office of director of this company was, for the above reasons, a "public office."

Was, then, the office held by the appellant a public office "within the United Kingdom"? As to this, I am completely satisfied by the reasoning of Lord Greene, M.R., in his judgment delivered in the Court of Appeal. I will only add that we are dealing with an "office," not with an "employment," the locality of which may be governed by different considerations. The office of director of an English company, the head seat and directing power of which is admitted to be in the United Kingdom, seems to me of necessity to be located where the company is. It is in fact part of the organic structure of the corporation. In such a case I do not think that it is true, as suggested by Rowlatt, J., in *Proctor v. Ryall*¹ that "the place of exercise governs." The appellant, though resident in the United States of America, while there held office in the United Kingdom; and though he may have taken his share of the directing power only in attending to the activities of the English Company in the United States of America and in Canada, he did so by virtue of his English office. From this point of view I think that too much emphasis may be laid upon the source from which the office was remunerated; but the fact that it was English reinforces the view that the locality of the office was in fact English. Like Lord Greene, M. R., I derive little assistance from previous cases. I consider it to be clear that the director of an English company which is resident in the United Kingdom wherever he resides and whether or not he takes any part in directing the affairs of the company, holds an office in the United Kingdom. For these reasons I am of opinion that the appeal fails and should be dismissed with costs.

My noble and learned friend, Lord Roche, wishes me to state that he concurs in the order proposed.

(1) (1928) 14 Tax Cas. 204, at p. 214.

LORD WRIGHT.—My Lords, the appellant was not resident in this country during the years of charge. Accordingly, the emoluments derived from his directorship in A. Wander Ltd., are not taxable unless they fall within the words of Schedule E nor are they affected by the provisions of the Finance Act, 1922, Section 18, because they could not have been charged under Schedule D. The Crown has, therefore, to establish that they are profits of a public office or employment within the United Kingdom, which last condition is specified in Rule 6.

Since Rule 6 (h) expressly includes offices or employments of profit under a corporate company, and since A. Wander Ltd., is a company registered in England under the Companies Acts, the requirements of Schedule E would seem so far to be satisfied. The company, further, is one which, as the case finds, is resident and controlled in the United Kingdom. I limit my observations to such a company, without considering what is the position of a company registered in the United Kingdom but controlled and managed abroad. The next matter to be examined is whether the directorship held by the appellant is an office or employment within the meaning of Schedule E. The word "office" is of indefinite content. Its various meanings cover four columns of the New English Dictionary, but I take as the most relevant for purposes of this case the following:

"A position or place to which certain duties are attached, especially one of a more or less public character."

This, I think, roughly corresponds with such approaches to a definition as have been attempted in the authorities, in particular *Great Western Ry. Co. v. Bater*¹ where the legal construction of these words, which have been in Schedule E since 1803 (43 Geo. 3, c. 122 Section 175), was discussed. It was there held that the position of a clerk in a railway company was not an office or employment of profit of a public nature within Schedule E. In *Great Western Ry. Co. v. Bater*¹ at p. 35, Lord Wrenbury was content so to hold without attempting to define what type of office or employment would satisfy the language of the Schedule. Lord Sumner, at p. 25 said that to hold otherwise would be an abuse of language. To hold that the director of a company, such as A. Wander Ltd., (though it is what is called a private company) does not have an office, within the meaning of the Schedule would equally, in my opinion, be an abuse of language. Everyone, I think, would say, that as director he held an office in the company. The word "employment" in my opinion, has to be construed with and takes its colour from the word "office."

(1) (1922) 2 A.C. 1.

If I may adopt the words of Lord Greene, M. R., it is too late to say that the director of a company like this does not hold an office within Schedule E. I do not attempt what their Lordships did not attempt in *Bater's Case*¹, i.e., an exact definition of these words. They are deliberately, I imagine, left vague. Though their true construction is a matter of law, they are to be applied in the facts of the particular case according to the ordinary use of language and the dictates of common sense, with due regard to the requirement that there must be some degree of permanence and publicity in the office. In *Bater's Case*¹ Lord Wrenbury seemed to disapprove of the opinion of Bankes, J., in *Berry v. Farrow*² that a director held an office within the schedule but I cannot think that his disapproval was justified or has been supported. In *Watson v. Rowles*³ a director of a "private" limited company was held to be taxable under Schedule E. The public character of the company is sufficiently established by its being incorporated under the statutory machinery of the companies Acts and by its being subject to the provisions of these Acts. It is, however, clear, that not all officers, and still less all employees, of a limited company or of any corporate body are holders of an office or employment under Schedule E. This is illustrated by *Bater's Case*¹ and much earlier by *Attorney-General v. Lancashire & Yorkshire Ry. Co.*⁴ I do not think that the agency considered in *Pickles v. Foster*⁵ was correctly treated as an office or employment within Schedule E.

There still remains the question whether the applicant's office or employment though it is public, is one within the United Kingdom as required by Schedule E, Rule 6. The Commissioners held that it was because the appellant retained the right and duty to exercise the power of a director. That decision was reversed by Lawrence, J., on the ground that the place of exercise governed. For that principle he relied on *Pickles v. Foster*⁵, and on the dictum of Rowlatt, J., in *Proctor v. Ryall*⁶. That dictum, however, was not necessary to the decision of the case and is qualified in its scope; e.g., Rowlatt, J., refers to the case of a sinecure which is not exercised anywhere at all. I do not think that Rowlatt, J., was right, if or so far as he held that the place of exercise governed.

The office of a director is something notional; its locality is one degree, if that is possible, even more notional. In my opinion the place where it is exercised, if it is exercised anywhere at all, is not necessarily the test. As obvious illustrations, I may refer to heads (d), (e), (f), under which come officers in the armed forces of the Crown.

(1) (1922) 2 A.C. 1.

(2) (1914) 1 K.B. 632.

(3) (1926) 95 L.J.K.B. 959.

(4) (1864) 2 H. & C. 792.

(5) (1913) 1 K.B. 174.

(6) (1928) 14 Tax Cas. 204.

To them Rule 18 (2) of the schedule clearly applies, at least as machinery for the assessment which is to be at the head office of the department. In any case, the words of Rule 1 are not simply "exercising" but "having or exercising" the office or employment. Exercising no doubt does involve activity in the office or employment, but a man may have an office and draw emoluments without doing any work at all. For instance, a director may in certain cases be properly allowed to retain his emoluments when for good reasons he may be relieved from any active duties at all. I have already mentioned the case of a sinecure. The peculiarity of this case is that the appellant has all the time been rendering in the United States and in Canada services of great value to the company, while at the same time he has been released from and has not performed the normal duties of a director, such as attendance at board meetings. He has still remained a director and as such cannot be in a different position from what he would have been in if he had not rendered those services abroad. I agree with Lord Greene, M.R., that it is in the office of director that the crucial test is to be found, because ".....every right which a director has and every duty which the law, general or special, imposes on him is to be exercised in this country and nowhere else."

That is the test accepted in substance by the Commissioners. It is, I think, the true test in a case like this. The appellant had or held all through the years of charge the office of director in the United Kingdom. That, in my opinion, is sufficient to satisfy the schedule.

The cases cited do not afford any strict parallel. In *Robinson v. Corry*¹, the taxpayer, who was deputy cashier at the naval base at Singapore, was not only outside the United Kingdom during the period of charge, but exercised all the duties of the employment there, as its nature required. Lord Greene, M. R., I think correctly treats the liability of the taxpayer there as depending on Rule 18 (2) which relates to employment under Government. *Pickles v. Foster*² could be sufficiently decided against the Crown on the ground that the agency in West Africa was not an office or employment within Schedule E. The ruling that the office or employment to come within Schedule E must be exercised in the United Kingdom was not necessary to the decision and cannot, I think, be supported. I think that the appeal should be dismissed.

LORD PORTER.—My Lords, I agree that this appeal should be dismissed. The appellant has been charged to tax under Schedule E in respect of a public office or employment of profit. Under the rules applicable to this schedule :

(1) (1934) 1 K.B. 240.

(2) (1913) 1 K.B. 174.

"(1) Tax under this schedule shall be annually charged on every person having or exercising an office or employment of profit mentioned in this schedule.....in respect of all.....fees.....

(6) the tax shall be paid in respect of all public offices and employments of profit within the United Kingdom or by the officers herein-after respectively described, namely : (h) offices or employments of profit under any company or society whether corporate or not corporate."

The appellant is a director of A. Wander Ltd., a private company which is resident and controlled in the United Kingdom. He was appointed a director by the articles of association and has no contract of service with the company. By article 90 the remuneration of the directors is a sum equal to ten (originally fifteen) per cent of the net profits of the company in every year, and is divisible among the directors in such proportion as they may agree, and, in default of agreement, equally.

Since 1912 the appellant has been resident in the United States of America, and in 1938 he became a naturalised American citizen. Mr. McMillan went to America to take over the management of a company in Chicago allied to the predecessors of A. Wander Ltd., for whom he opened a Canadian office, and concerned himself in the administrative and selling organisation there. In 1930, largely as a result of his advice, a Canadian factory was built. Mr. McMillan superintended its building and has since that time continued to advise its manager on matters relating to the conduct of the business. The appellant, as managing director of the Chicago company consults with the managing director of the English company, or any other director of the latter company when they are in Chicago, regarding anything to the advantage of the English, Chicago or Canadian businesses, and has assisted in Canada in engaging the Canadian staff. Copies of all minutes, annual balance sheets and managing directors' and auditors' reports of A. Wander Ltd., are sent regularly to the appellant in America but he has attended no board meetings in England except one in 1931, and only one in Chicago in 1925. He is not required to attend board meetings of the English company. Indeed, notice of such meetings are not sent to him.

In these circumstances, he was assessed by the Commissioners in respect of his income as director of the English company under the Income-tax Act, 1918, Schedule E, for the years 1937-38 and 1938-39, but, being dissatisfied with the decision in point of law, required a case to be stated.

The case from which the facts I have set out are taken was heard first by Lawrence, J., who overruled the Commissioners, and afterwards

by the Court of Appeal, who restored their assessment. Your Lordships have to determine if they were right in so doing.

The points taken on behalf of the appellant were (i) that the office was not within the United Kingdom, and (ii) that it was not public.

For the first point reliance was placed upon the decisions in *Pickles v. Foster*¹ and *Proctor v. Ryall*². The result of those cases was said to be that an office was not within the United Kingdom unless it was exercised there; and the appellant went on to argue that on the facts found he did not exercise his office in this country.

The Crown did not dispute, and, indeed, I think it is plain, under the rules applicable to Schedule E, that tax is charged only on persons having or exercising an office mentioned in the Schedule, and the only offices mentioned in the Schedule are those within the United Kingdom. If therefore, the office is not within the United Kingdom, it is not the subject of tax under this Schedule.

Though they made this admission, the respondents did not accept the view that the office must be exercised within the United Kingdom. Whether a person, who holds the office of director in a company resident and managed and therefore controlled in this country, who receives his fees from a pool provided in this country for himself and his co-directors—a pool divided up in the proportions which they agree—and who receives copies of minutes, annual balance sheets and managing directors' and auditors' reports, exercises or does not exercise his office in this country is a question which I do not think it necessary to decide. In the two cases quoted the problem was expressed with sufficient accuracy by asking, was the employment exercised here or not; no question of *having an office* arose. It does arise in the present case, and whatever views one may entertain as to the accuracy of the language used in the cases referred to above when applied to those individual cases, it is not, I think, intended to apply to all cases under Schedule E.

For the present purpose it is enough to say that a person in the position of the appellant holds an office in this Kingdom despite the fact that he has not in fact attended any meetings in this country since 1931. He is a director of a company resident and managed in this country, entitled to attend any board meetings which may be held here, giving advice as to matters concerning its management and supplied at least with its formal literature. In such a case it is, I think, immaterial that most, if not all, of Mr. McMillan's activities are carried out in America. He still holds an office in the United Kingdom.

If the appellant is, as I think he is, wrong on this point, he still has a second string to his bow. Even, he says, if he has or exercises

(1) (1913) 1 K. B. 174.

(2) (1928) 14 Tax Cas. 204.

an office in the United Kingdom, it yet is not a public one. That it is an office is, I think, plain. It has permanency apart from the temporary holder and is held in one of the specified corporations. One has only to refer, for example, to the Companies Act, 1929, Sections 145 and 151, to find the phrase office of director expressly mentioned. Indeed, this is not in dispute. What is controverted is the allegation that a directorship, at any rate in a so-called private company, is a public office. The argument is put upon the ground that at worst—i.e., at worst for the appellant-directors, in the case of companies not by statute requiring any directors, if appointed at all (as they may be, but are not compelled to be in the case of a private company), are not holders of a public office.

There is no magic in the phrase private company. It is true that it need not have directors or issue a prospectus; that it is not permitted to have more than 50 shareholders and may have no more than two; but it still must be registered and keep an official register of its members. It is a corporate body constituted by Act of Parliament (now the Companies Act, 1929), and that Act imposes duties upon the office itself and its holder for the time being. The obligations are imposed in the public interest in order that some public control over its organisation and activities may be obtained. No doubt less control is exercised in the case of a private than in the case of a public company; but the former is not private in the sense that it has no public formalities to carry out, and the word private is only used as a convenient label to distinguish it from the so called public company. I think the office is a public one, and I agree with the motion proposed by Viscount Simon, L. C.

Appeal dismissed.

[KING'S BENCH DIVISION.]

LEADER v. COUNSEL (INSPECTOR OF TAXES).

BENSON v. COUNSEL (INSPECTOR OF TAXES).

LAWRENCE, J.

January 19, 20, 1942.

INCOME—PURCHASE OF RACE-HORSE—RECEIPTS FROM THE SALE OF FREE NOMINATIONS BY SUBSCRIBERS—WHETHER INCOME—INCOME TAX ACT, 1918 (8 & 9 GEO. 5, c. 40) SCH. D, CASE VI.

Under a written agreement certain race-horse owners subscribed a sum for the purchase of stallion and for working capital, and the subscribers were entitled to send mares to the stallion free in proportion

to the number of their shares. The management of the horse was left in the hands of a committee but the horse was not kept on the land of any one of the subscribers. Some of the subscribers did not have mares which were considered suitable by the committee, or had mares which they did not want to send to him, and these owners were able to sell their free nominations to other persons. The Special Commissioners assessed under Case VI of Schedule D of the Income Tax Act, 1918, the receipts from the sale of nomination by two of the subscribers; but they found that the subscribers were not carrying on a trade:

Held, that the transactions in question were not a purchase and a re-sale of property, but were merely a realisation of the reproductive faculties of the stallion. There was no purchase of the nominations which were sold, the only purchase in which they entered being that of the race-horse. Consequently the receipts from the sale of the nominations were in the nature of income.

Cases referred to:—

Cooper v. Stubbs (1925) 2 K.B. 753; 94 L.J.K.B. 903; 133 L.T. 582; 10 Tax Cas. 29.

Jones v. Leeming (1930) A.C. 415; 99 L.J.K.B. 318; 143 L.T. 50; 15 Tax Cas. 333.

Pearn v. Miller (1927) 11 Tax Cas. 610.

Ryall v. Hoare; Ryall v. Honeywill (1923) 2 K.B. 447; 92 L.J.K.B. 1010; 129 L.T. 505; 8 Tax Cas. 521.

Appeals from the Special Commissioners of Income Tax.

The facts are fully set out in the judgment.

J. H. Bowe, for the appellants.

The Solicitor General (Sir William Jowitt, K. C.), and Reginald P. Hills, for the respondent.

JUDGMENT.

LAWRENCE, J.—The Special Commissioners have assessed the appellants under Schedule D, Case VI, although they have found that the appellants were not carrying on a trade in respect of the horse Solario, with which the case is concerned. The facts are that in 1932, on the death of Sir John Rutherford, who was the owner of this famous horse, Solario was going to be sold, and a number of race-horse owners decided that they would like to join together in order to prevent Solario being taken out of the country. Accordingly, they empowered Lord Glanely to bid for Solario on their behalf up to £30,000. As a matter of fact, Lord Glanely went beyond that limit and acquired Solario for £47,000, subject to 37 nominations which were already in existence. After this purchase, the racing owners, who had authorised Lord Glanely to bid, made a written agreement under which 24 of them subscribed a sum of £53,000, £47,000 for the price of the horse and the remainder for what is called working capital. Each owner took a

certain number of shares, one owner taking some shares which he held on behalf of other people. In accordance with the agreement, they were entitled to send mares to Solario free in proportion to the number of their shares, but the management of the horse was left in the hands of a committee of three, and they were empowered to regulate the number of mares which Solario might serve, the price at which he was to stand, and the suitability of the mares which might be sent to him. It therefore happened that certain of the subscribing owners might not, and did not, have mares which were considered suitable, or, at any rate, they possibly did not want to send to him, and in those circumstances these owners were able to sell their free nominations to other persons who might have mares which were suitable and which would be acceptable to the committee. The question in the case is whether or not the receipts which the two appellants had over the six years, 1934 to 1940, are taxable under Schedule D, Case VI, the Special Commissioners having held that they are, although they found that the appellants were not carrying on a trade.

The argument for the appellants is based on the decisions in *Pearn v. Miller*¹ and *Jones v. Leeming*², and, in particular, on the dictum of Lawrence, L. J., in the latter case, when he said; "It seems to me that, in the case of an isolated transaction of purchase and resale of property, there is really no middle course open. It is either an adventure in the nature of trade, or else it is simply a case of sale and resale of property."³ It is conceded that the facts here do not show an isolated transaction, but counsel for the appellants has contended that the transfer of these nominations to other persons in return for money is a purchase and resale of property within the meaning of the dictum of Lawrence, L. J., and that, therefore, as the Commissioners have found that there was no trade carried on, the profits cannot be taxed under case VI. To this argument counsel for the Crown has replied that the facts show, not a purchase and resale of property, but merely the user of the property which the subscribing owners acquired in Solario, and that the receipts derived from the user are in their nature revenue or income. Counsel for the appellants, in reply, contended that this was not the true view, because the rights of the appellants were not the unfettered rights of the owners or part owners, but were limited to a considerable extent by the terms of the agreement made between the owners.

In my opinion, the argument for the Crown is correct. As appears from the authorities, where the Commissioners have found that there is

(1) (1927) 11 Tax Cas. 610.

(2) (1930) A. C. 415.

(3) (1930) 1 K. B. 279, 302.

no trade, the true question to be considered is whether the receipts in question are of the nature of income or revenue. That is indicated in *Ryall v. Hoare*¹ where Rowlatt, J., said: "First, anything in the nature of capital accretion is excluded as being outside the scope and meaning of these Acts, confirmed by the usage of a century. For this reason, a casual profit made on an isolated purchase and sale, unless merged with similar transactions in the carrying on of a trade or business is not liable to tax. 'Profits or gains' in Case VI refer to the interest or fruit as opposed to the principal or root of the tree".² Those observations seem to me to be applicable to this case, for the facts here do not show an accretion of capital. These receipts, therefore, were in the nature, not of capital, but of interest being the fruit of the tree. The receipts in *Ryall v. Hoare*¹ which were commissions earned for guaranteeing an overdraft, were held to be taxable. In *Pearn v. Miller*³ the subject had bought seven pieces of real property, subsequently reselling them at a profit and, the Commissioners having found that he was not carrying on a trade, the question was whether the accretion in value of those properties was taxable under Case VI. Rowlatt, J., said "I wish to say very clearly, in order that I may be corrected if I am wrong, that I think it is very often the case that you may say of something that it may be under Case I or Case VI. That may very often be true, but it is wholly illusive to say anything of that kind where you are dealing with a difference between the purchase and sale price of goods. If it is desired to tax the difference between what a man has bought goods for, or property for, and sold them for, you can only tax it, in my judgment, if you can say that what he did was a trade or adventure or concern in the nature of trade. I think you cannot get under Case VI a tax out of appreciation of property; you have to get it under Case I."⁴ Rowlatt, J., was there dealing with the purchase and resale of real property, but it is clear from what he said, that the same argument applies to the purchase and resale of goods.

In my opinion, however, there is nothing like a purchase and resale of goods or of any other property to be found in the transactions which gave rise to the receipts in question in the present case. The appellants did not buy the right to their nominations. They bought the horse. It is accurate to say that they sold the right to the nominations, but that was merely a way of realizing the fruit of the purchase of the horse. In *Jones v. Leeming*⁵, another case of the purchase and resale of real estate, the Law Lords put the matter in very much the same way, though they referred to the dictum of Lawrence, L.J., which

(1) (1923) 2 K. B. 447.

(2) (1928) 2 K. B. 447 at p. 454.

(3) (1927 11 Tax Cas. 610,

(4) (1927) 11 Tax Cas. 610. at p. 613.

(5) (1930) A. C. 415.

I have quoted. Lord Buckmaster said: "Can the profits made in this case be described as income? Where the respondent a company promoter or were his business associated with purchase and sale of estates, wholly different considerations would apply, but this is negatived; the transaction in this case stands isolated and alone. It is, to my mind, in the circumstances, purely an affair of capital. I can see no difference between it and what might have happened had the respondent bought shares in two companies which were going to be amalgamated, and then sold equivalent shares in the amalgamated company at a profit; an accretion to capital does not become income merely because the original capital was invested in the hope and expectation that it would rise in value; if it does so rise, its realization does not make it income."¹ Lord Warrington, who had been a party to the decision in *Cooper v. Stubbs*², said about that case what, in my opinion, lays down the true principle: "The nature of the profit must in each case be considered. If it arises from a trade within the definition in the Act, no difficulty occurs. If it does not, I know of no better criterion than that adopted by the majority of the Court of Appeal in *Cooper v. Stubbs*² and by Lawrence, L.J., in the present case. This is expressed by Atkin, L.J., in *Cooper v. Stubbs*² as follows: 'Annual profit or gain'to my mind must mean something which is of the nature of revenue or income'. In *Cooper v. Stubbs*² the Court of Appeal were concerned with transactions entered into by cotton brokers for dealing in futures in cotton, and they held that, although the Commissioners had found there was no trade being carried on by the brokers, the transactions in question being carried out privately and apart from their firm, yet they were taxable in respect of the receipts which they derived therefrom under Case VI, because they were of a revenue or income nature. It is clear from the judgment that, although it was not the intention of the brokers that they should take delivery of the cotton, the contracts which they made were real, enforceable and legal contract by virtue of which they might have had to take delivery of the cotton. If, therefore, the dictum of Lawrence, L.J., in *Leeming v. Jones*³ has the full effect claimed for it by counsel for the appellants in the present case, it would have been impossible for the Court of Appeal to have arrived at their decision in *Cooper v. Stubbs*² which was approved by the House of Lords in *Jones v. Leeming*.

The true principle applicable here is that laid down in *Cooper v. Stubbs*² namely, that where there is no trade it must be seen whether the receipts are of an income or revenue nature, and, if they are, they

(1) (1930) A.C. 415, at 419.

(3) (1930) 1 K.B. 279, 302.

(2) (1925) 2 K.B. 753, at 775.

can be be taxed under Case VI, although they may be said to be from some aspects the purchase and resale of property. In the case before the court the transactions in question were not a purchase and a resale of property, but were merely a realization of the reproductive faculties of Solario. There was no purchase of the nominations which were sold. The only purchase into which the appellants entered was that of the horse itself. For these reasons, in my opinion, the decision of the Commissioners was correct and the appeal must be dismissed.

Appeal dismissed

[KING'S BENCH DIVISION.]

HOBBS v. HUSSEY (H. M. INSPECTOR OF TAXES).

LAWRENCE, J.

January 27, 28, February 18, 1942.

INCOME—SALE OF COPYRIGHT IN LIFE STORY OF SOLICITOR'S CLERK—ISOLATED TRANSACTION—WHETHER TRANSACTION A PERFORMANCE OF SERVICES—SUM RECEIVED—WHETHER INCOME.

The assessee, a solicitor's clerk, who had never carried on the profession of an author, was assessed under Case VI of Schedule D in respect of a sum of money received from the sale to a newspaper of the serial rights in his life story. It was contended on his behalf that the transaction was a sale of the copyright of the series of articles and, therefore, resulted in the realisation of capital:

Held, that the transaction was the performance of services by the appellant, the sale of the copyright being subsidiary thereto, and that therefore the payments were in the nature of income assessable under Case VI.

Cases referred to:

Trustees of Earl v. Commissioners of Inland Revenue (1939) 22 Tax Cas. 729; 1939 S.C. 676.

Ryall v. Hoare (1923) 2 K.B. 447; 8 Tax Cas. 521; 92 L.J.K.B. 1010; 129 L.T. 505; 39 T.L.R. 475.

Martin v. Lowry (1927) 11 Tax Cas. 297; (1927) A.C. 312; 95 L.J.K.B. 497; 135 L.T. 523; 42 T.L.R. 233.

Sherwin v. Barnes (1931) 16 Tax Cas. 278.

Case stated under Section 49 of the Income-tax Act, 1918, by the Commissioners for Special Purposes of the Income Tax Acts.

N. E. Mustoe, for the Appellant.

The Solicitor General (Sir William Jowitt, K. C.) and Reginald P. Hills, for the Crown.

JUDGMENT.

LAWRENCE, J.—In this case the Special Commissioners have held that the appellant, a Solicitor's clerk, who has never carried on the

porfession of an author, is assessable under Case VI of Schedule D in respect of a sum of money received from *The People* newspaper for the serial rights in his life story.

It was contended for the appellant that the transaction was a sale of the copyright of the series of articles and, therefore, resulted in the realisation of capital and not a revenue receipt, and the case of *Trustees of Earl Haig v. Commissioners of Inland Revenue*¹, was relied on.

The Solicitor-General, whilst not admitting that Earl Haig's Trustees case was rightly decided, argued that it is distinguishable; and that it was settled by *Ryall v. Hoare*², so far as Courts of first instance are concerned, that profits from a single article by a person who is not an author are assessable under Case VI of Schedule D. He also submitted that the true question in such cases is whether the transaction in question is really a sale of property or the performance of services, and that the present transaction falls into the latter category and profits therefrom are therefore of a revenue nature.

In my opinion, the test suggested is correct. Any sale of property where no concern in the nature of trade is carried on must result in the realisation of capital (compare *per* Rowlatt, J., *Ryall v. Hoare*³); and it is also true, in my opinion, that the performance of services, though they may involve some subsidiary sale of property (*e. g.*, dentures sold by a dentist), are in their essence of a revenue nature, since they are the fruit of the individual's capacity which may be regarded in a sense as his capital but are not the capital itself. Does then the fact that the present transaction involved the sale of the copyright in the appellant's series of articles, constitute the profits therefrom capital; or is such sale merely subsidiary to what was in its essence a performance of services by the appellant? In my opinion the true nature of the transaction was the performance of services. The appellant did not part with his notes or diaries or his reminiscences. He could re-publish the very articles themselves so long as they were not in serial form, and on the whole I am of opinion that the profits he received were of a revenue nature and not the realisation of capital. In the case of *Earl Haig's Trustees*¹, the facts were, of course, totally different. The trustees possessed diaries of unique importance and great value, and the view of the Court of Session was that these diaries were capital assets and that the trustees had realised some part of such assets. The Court had not to consider the profits received by the author of the book; nor could it be said that from the point of view of the trustees, the sale was subsidiary to the performance of services by them.

(1) (1939) 22 Tax Cas. 725: (2) (1923) 8 Tax Cas. 521. (3) (1923) 8 Tax Cas. 521 at 525.

In any event, in view of the decision of *Ryall v. Houre*¹ approved, as it was, in the Court of Appeal in *Martin v. Lowry*² and adhered to by Rowlatt, J., in *Sherwin v. Barnes*³, I consider that I ought to follow the dicta of Rowlatt, J., which are directly in point and were approved by the Court of Appeal.

The appeal will, therefore, be dismissed with costs.

Appeal dismissed.

[IN THE HOUSE OF LORDS.]

FATTORINI (THOMAS) (LANCASHIRE), LTD.

v.

INLAND REVENUE COMMISSIONERS.

THE LORD CHANCELLOR (VISCOUNT SIMON), LORD PORTER.

Feb. 10, 12, 13, 16. April 27, 1942.

SURTAX—COMPANY—LOAN FROM BANK CHARGING DIVIDENDS—WHETHER INCOME UNREASONABLY WITHHELD FROM DISTRIBUTION—FINANCE ACT, 1922 (12 & 13 GEO. 5, c. 17), SEC. 21*—FINANCE ACT, 1937 (1 EDW. 8 & 1 GEO. 6, c. 54), SEC. 14 (2) (a).

Before February 22, 1936, the appellant company, a purely investment company, held investments for which it had paid over £18,000 and which were producing revenue. On that date F. and his wife, the only shareholders and directors of the company, acquired large holdings in other companies, and for that purpose entered into an agreement with a bank under which the bank undertook to advance £108,000 at a stipulated rate of interest. With that advance, supplemented by the company's own cash, the company acquired the shares of the operative company for £ 121,221. The bank's loan was secured by a deposit of all the shares, including the investments already owned by the investment company, and the company bound itself to pay to the bank, until the loan was completely discharged, all dividends which it received in respect of any of its investments. Those dividends were the company's sole source of income. In the financial year 1936-37 the income from all its investments was £6,540, and in the year 1937-38 was £ 84,855, all of which was paid over to the bank. The appellant company declared no dividend during or in respect of those two years. The Special Commissioners, acting under the powers conferred on them by Section 21 of the Finance Act, 1922, as amended, directed that, for the purpose of assessment to surtax of the members of the company, the total income from all sources of the company for the years of assessment 1936-37 and 1937-38

(1) (1923) 8 Tax Cas. 521.

(2) (1926) 11 Tax Cas. 297.

(3) (1931) 16 Tax Cas. 278.

*This section corresponds to Sec. 23A of the Indian Income-tax Act.

respectively (see Section 14 (2) (a) of the Finance Act, 1937), should be deemed to be the income of the members of the company and that the amount should be apportioned among them. That decision, after appeals to the Special Commissioners in their judicial capacity, the Board of Referees, and Macnaghten, J., was confirmed by the Court of Appeal. Before the House it was no part of the case for the Revenue that the company should not have entered into the agreement with the bank. That agreement was admitted not to have been made with any view of avoiding surtax:—Held, (1) that the contract with the bank did not bind the company not to distribute a dividend, as the company made profits in each of the financial years in question, and the fact that it used the dividends (as it was bound to do) in reducing the charge on the shares, did not make it unlawful to distribute a dividend (*MONTAGUE BURTON, LTD. v. INLAND REVENUE COMMISSIONERS* [1936] (105 L.J.K.B. 286), *GLAZED KID, LTD. v. INLAND REVENUE COMMISSIONERS* [1930] (15 Tax Cas. 445); (2) by the HOUSE, that it did not follow that because the company was purely an investment company its profits should have been distributed to its shareholders. The additional investments were highly profitable and there was no evidence that the company could have financed its purchase on less onerous terms, and it was no part of the case for the Revenue that the company should not have entered into this bargain with the bank; and (3) that there was no evidence to support the finding of the Board of Referees that the company had not, in the circumstances, within a reasonable time distributed in the manner referred to in Section 21 of the Finance Act, 1922, a reasonable part of its income for either of the periods in question, as the company had followed a reasonable course in making its agreement with the bank and there was no evidence that it was commercially possible for the company to borrow the necessary amount to pay the dividends.

Per LORD ATKIN and LORD WRIGHT.—The onus of proof to show that the company acted unreasonably in withholding part of its income from distribution was on the Crown, as Section 21 was penal in character.

'Actual income' does not mean the specific receipts that come in from time to time but the 'income-tax income' as calculated at the end of the year of assessment.

Decision of the COURT OF APPEAL reversed.

Cases referred to:—

Bomford v. Osborne (1941) 110 L.J.K.B. 462; (1942) A.C. 14; 10 I.L.R. Suppl. 27.

Glazed Kid, Ltd. v. Inland Revenue Commissioners (1930) 15 Tax Cas. 445.

Inland Revenue Commissioners v. Blott; *Same v. Greenwood* (1921) 90 L.J.K.B. 1028; (1921) 2 A.C. 171; 8 Tax Cas. 101.

Montague Burton, Ltd. v. Inland Revenue Commissioners (1934) 152 L.T. 8; 20 Tax Cas. 48; affirmed in *H. L.* (1936) 105 L.J.K.B. 236; 154 L.T. 355; 4 I.T.R. Suppl. 12.

Appeal from an Order of the Court of Appeal dated August 2, 1940.

The necessary facts are set out in the headnote.

Tucker, K. C., and S. Terence Donovan, for the appellants.

The Solicitor-General (Sir William Jowitt, K.C.) and R.P. Hills, for the respondents.

The arguments sufficiently appear from the judgments.

Their Lordships took time for consideration.

THE LORD CHANCELLOR.—This appeal arises out of a case stated for the opinion of the High Court by the Board of Referees under paragraph 2 of the First Schedule to the Finance Act, 1922. The appellant is a company "under the control of less than five persons" to which Section 21 of that Finance Act applies. The company is purely an investment company and before entering into the transactions next to be stated held investments for which the company had paid over £18,000, and which were producing revenue.

Those controlling the company were Mr. Wilfred Fattorini and his wife; they were, as I understand, the only shareholders and were the directors of the company. It was desired to increase the investments held by the company by acquiring certain large holdings of shares in other companies (which have been called "the operative companies" to distinguish them from the investment company), but the appellant company had no sufficient resources of its own by means of which to make the purchase. Accordingly, it approached Martins Bank, Ltd., and on September 22, 1936, an agreement was made under which the bank undertook to advance a sum not exceeding £108,000 at a stipulated rate of interest. With this advance, supplemented by its own cash, the company acquired the shares of the operative companies at a price of £121,221. The bank's loan was secured by a deposit of all the shares, including the investments already owned by the company, and the company bound itself to pay to the bank, until the loan was completely discharged, all dividends which it received in respect of any of its investments. These dividends were the company's sole source of income. The investments in the operative companies' shares brought in an excellent return; in the financial year 1936-37 the income from all investments was £6,540; and in the financial year 1937-38 no less than £34,855. These amounts were paid over to the bank in accordance with the agreement with the result that the bank loan was proportionately reduced.

The appellant company declared no dividend during or in respect of the two years above referred to. The Special Commissioners, acting under the powers conferred upon them by Section 21 of the Finance Act, 1922, as amended, directed that for the purpose of assessment to

surtax, the total income from all sources of the company for the years of assessment 1936-37 and 1937-38 respectively (see Section 14 (2) (a), Finance Act, 1937) should be deemed to be the income of the members of the company, and that the amount should be apportioned among them. The company appealed to the Special Commissioners in their judicial capacity against such direction, and the Special Commissioners allowed the appeal and discharged the direction for both years. The respondents required the appeal to be reheard by the Board of Referees which, subject to the case stated, reversed the decision of the Special Commissioners and restored the direction. The Special case came before Macnaghten, J., who delivered judgment reversing the determination of the Board of Referees and restoring that of the Special Commissioners. From this decision the respondents appealed to the Court of Appeal (Scott, L. J., Clauson, L. J., and Goddard, L. J.) which reversed the decision of Macnaghten, J., and restored the determination of the Board of Referees. There has thus been a constant alternation of view in the course of this litigation, each tribunal in turn reversing the decision brought to it on appeal.

Counsel for the appellant, in his excellent argument, placed before the House the statutory history of successive efforts made by the Legislature to prevent the avoidance of super-tax, or of its successor surtax, by using the cloak afforded by company law. Since the tax is charged only in respect of the income of an individual, its incidence might be avoided by transferring to a company controlled by such individual, in return for shares, the source of such income and by securing that, instead of any dividends being declared, the profits made by the company should be accumulated and ultimately distributed in a capital form as the results of voluntary liquidation or by creating bonus shares (*Inland Revenue Commissioners v. Blott*; *Same v. Greenwood*¹) or otherwise. Accordingly, by Section 21 of the Finance Act, 1922, it was enacted: "With a view to preventing the avoidance of the payment of super-tax through the withholding from distribution of income of a company which would otherwise be distributed, it is hereby enacted as follows:

"(1) Where it appears to the Special Commissioners that any company to which this section applies has not, within a reasonable time after the end of any year or other period ending on any date subsequent to the fifth day of April, nineteen hundred and twenty-two, for which accounts have been made up, distributed to its members in such manner as to render the amount distributed liable to be included in the statements to be made by the members of the company of their total

(1) (1921) 2 A.C. 171; 8 Tax Cas. 101.

income for the purposes of super-tax, a reasonable part of its actual income from all sources for the said year or other period, the Commissioners may, by notice in writing to the company, direct that for purposes of assessment to super-tax, the said income of the company shall, for the year or other period specified in the notice, be deemed to be the income of the members and the amount thereof shall be apportioned among the members :

“Provided that, in determining whether any company has or has not distributed a reasonable part of its income as aforesaid, the Commissioners shall have regard not only to the current requirements of the company's business but also to such other requirements as may be necessary or advisable for the maintenance and development of that business.”

The First Schedule to the Act of 1922 (para. 6) provides that “actual income from all sources” is to be computed by reference to the income for the year in question, and not to that of a past period. In order to complete the statutory scheme as it applied to the years 1936-37 and 1937-38, it is necessary to add a reference to the Finance Act, 1927, Section 31, and the Finance Act, 1936, Section 20. These later enactments, however, do not affect the present case, since the shares of the operative companies purchased as the result of the agreement of September 22, 1936, were not the first property of a substantial character acquired by the investment company, and moreover the loan was from a bank.

Counsel pointed out that the Legislature has now, in the case of some investment companies, made it more difficult to escape the burden of surtax (see Finance Act, 1939, Section 14 (1)), but this is outside the period within which the present dispute falls, and it must not be assumed as a matter of statutory construction that earlier provisions have a particular meaning because if so interpreted the need for the later enactment is elucidated.

The paragraphs of the special case which raise the matters now to be decided are the following: “23. We the members of the Board sitting to rehear the appeal hold as a matter of construction of the contract with Martins Bank that it would not have been a breach of contract for the company to distribute a dividend and we found as a fact that if we were wrong on this point and a distribution of a dividend would have been a breach of contract it was not reasonable for the company to make such a contract. We hold that the case of *Glazed Kid, Ltd. v. Inland Revenue Commissioners*¹ was distinguishable, as it was assumed in the judgment in that case that the distribution of a

(1) (1930) 15 Tax Cas. 445.

dividend could only have been made if moneys payable to the bank had been retained, a course which would have been restrained by injunction ; and there appeared to be no argument that the contract was not a reasonable contract. 24. We considered that as the company was an investment company, which after August 24, 1936, held investments producing revenue for which the company had paid £18,000, there was *prima facie* case that the reasonable course was that the company should so manage its affairs as to provide for distribution of dividend ; and that the company had not displaced such *prima facie* case by evidence that this could not have been done without jeopardising the interests of the company or without making it impossible to acquire the shares which it desired to buy. 25. We found as a fact that the company had not within a reasonable time distributed in the manner referred to in Section 21 of the Finance Act, 1922, a reasonable part of its income for either of the periods in question." And the questions for the opinion of the Court are thus stated : "(1) Whether our conclusions of law as set forth in paragraph 23 were correct. (2) Whether there was evidence to support our finding of fact as set forth in paragraph 25. (3) Whether the matters set forth in paragraph 24 are such as to show that we misdirected ourselves as to the onus of proof in a case where it is admitted that an investment company with a substantial income has not distributed any part of it."

As regards paragraph 23, I agree that the contract with the bank did not bind the company not to distribute a dividend, and inasmuch as the company made profits in each of the years in question, the fact that it used the dividends it received (as it was bound to do) in reducing the charge on the shares, did not make it unlawful to distribute a dividend. There is nothing in law to prevent a company using an income-receipt as cash in its hands to discharge a capital liability or to purchase a capital asset, and then, after the close of its financial year, paying a dividend out of other cash or borrowing for the purpose, to the extent of the credit balance standing on profit and loss account. This was very clearly explained by my noble and learned friend Lord Romer, when sitting in the Court of Appeal in *Montague Burton, Ltd. v. Inland Revenue Commissioners* (152 L.T., at p. 16 ; 20 Tax Cas. at p. 70), and his view was affirmed on appeal to this House, particularly in the speeches of the Lord Chancellor (Lord Hailsham), and of Lord Russell of Kilowen (105 L.J.K.B. at pp. 237, 240 ; 20 Tax Cas. at pp. 74-77). The Board of Referees sought to distinguish the decision of Rowlatt, J., in *Glased Kid, Ltd. v. Inland Revenue Commissioners*¹, where the company made a very similar arrangement to borrow from a bank the purchase price

(1) (1930) 15 Tax Cas. 445.

of shares, on the terms that it paid over to the bank the dividends as received. Macnaghten, J., in reversing the decision of the Board of Referees, declared himself unable to see the distinction; and I agree with him. Rowlatt, J.'s judgments in income-tax cases deserve, in my opinion, particular attention, but in this instance, with all respect to that learned Judge, his view cannot be upheld. He said: "It is not open to anyone to say that they" (the Glazed Kid Company) "have not distributed a reasonable part when they could not distribute any part of what were their profits, because every penny of those profits, which solely consisted of these dividends, were under contract receivable by somebody else." This is to confuse the use made of an income-receipt to discharge a capital liability with the quite distinct question of the use of a credit balance on the profit and loss account to justify the distribution of a dividend.

As for paragraph 24 of the special case, the Commissioners had contended before the Board of Referees that as the company was purely an investment company, its profits should have been distributed to its shareholders. I do not think that this general proposition can be sustained; as already pointed out, the additional investments were highly profitable. There was no evidence that the company could have financed its purchase on less onerous terms, and the Solicitor-General rightly admitted that it was no part of the case for the Revenue before this House that the company should not have entered into this bargain with the bank. As Scott, L.J., observed, a finding that it was "not reasonable to make such a contract" is irrelevant.

There remains paragraph 25, which contains a finding of fact in the exact terms which would justify the Commissioners' direction under Section 21. The question to be decided is whether there was evidence to support this finding of fact, and the answer to that question must be found by examining the contents of the case and of the annexed documents. The case does not state what the evidence was upon which the Board of Referees relied in coming to this conclusion. If the finding in paragraph 25 is to be treated as based upon the Board's view, expressed in paragraph 24, that the company had not followed a reasonable course in making its agreement with the bank, then this view, as I have already pointed out, would not provide a firm foundation for the conclusion. Apart from this, the only material upon which the conclusion in paragraph 25 can be regarded as based is the fact, to be deduced from the documents, that the company might still pay a dividend if it could borrow the necessary amount on the equity of redemption of the deposited shares. This would be an unusual proceeding, and there is no evidence referred to in the case that it would be

commercially possible for the company to do so, or to support the view that, in the circumstances, the failure to do so would amount to a failure to distribute a reasonable part of the company's actual income. I do not forget that the Board of Referees is a tribunal of business men capable of applying a business judgment to the question before them, but I find it impossible to say that the case contains conclusions of fact which will support the finding in paragraph 25, when in truth no such conclusions are formulated at all. There is no evidence on the matter to be found in the case; and in the absence of material adequate to support the conclusion, I think the House is bound to answer the question put in the negative and to allow the appeal.

I move that the appeal be allowed with costs.

LORD ATKIN stated the preliminary facts, read Section 14 (2) of the Finance Act, 1937, and continued: By the appropriate sections dealing with appeals the Board of Referees on appeal take the place of the Special Commissioners and can give the statutory direction. The Board are a special tribunal appointed indeed by the Treasury; though not to be lions under the Treasury chair, but to decide disputes judicially between Crown and subject, holding the scales impartially between them. No criticism at all has been directed against them in this respect. Their findings of fact are final; and their decisions can only be questioned on case stated on points of law. I must deal as briefly as possible with the facts stated before discussing the points of law raised in this case. The appellant company was incorporated in 1919 with a nominal capital of £25,000 divided into 15,000 ordinary and 10,000 preference shares of £1 each, of which 15,000 ordinary and 1,765 preference shares have been issued as fully paid up. The company was formed to acquire a retail jewellery and mail order business carried on at Bolton by Thomas Fattorini, and in June, 1919, it duly acquired the business for £14,724 paid as to £12,000 in fully paid shares and the balance in cash. There were at this time three other companies in existence in each of which Thomas Fattorini was the principal shareholder: (1) Thomas Fattorini (Skipton), Ltd., incorporated in 1919 with an issued capital at the material date of 47,980 ordinary and 4,200 preference shares of £1 each. (2) Thomas Fattorini (Birmingham), Ltd., afterwards named Thomas Fattorini, Ltd., with an issued capital of 13,480 ordinary shares of £1 each. (3) H. Pearson, Ltd., with an issued capital of 24,980 shares of £1 each. Company No. 1 carried on a jewellery and mail order business at Skipton. Company No. 2 carried on the business of manufacturing medals and badges at Birmingham. Company No. 3 carried

on the business of cycle dealers. Thomas Fattorini did not acquire his interest in this company until November, 1919. In 1924 the cycle business ceased and the company thereafter carried on a mail order business in Manchester.

In 1928 the appellant company discontinued its jewellery business, and sold its mail order business to company No. 1 for £14,000, which it lent to one or other of the three operative companies named. From that date up to at any rate 1936, it carried on a blameless existence as an investment company, distributing annually dividends of about £500 or £600 derived from the interest on the above loans. In the company as stated Thomas Fattorini was the principal shareholder, the other being apparently his son Wilfred. In June, 1934, Thomas Fattorini died and his son Wilfred acquired his father's shares in the appellant company, being registered in respect of them in September, 1936. After that date he and his wife were the sole shareholders in the company. In the same year the company proceeded to buy the shares held by the executors of the father and by his other son in the three above-named operative companies. The shares held by Frank were bought from him by an agreement made in the early part of 1936. The total price was £18,229, which the company paid out of its own resources, realising the loan for that purpose.

The shares were transferred in August, 1936. At the same time the company proceeded to buy the remaining shares in the operative companies, namely, those held by the executors of the father and by Wilfred himself. For these shares the price required amounted to a large sum, over £100,000, and it was necessary to get the assistance of the company's bank to finance the transaction. These further shares amounted to 77,300, and the price to be found was about £105,000, so that the shares were bought at a premium. Accordingly, the bank agreed to provide the necessary overdraft. They took as security all the shares in the operative companies, both those now to be purchased and those already purchased from Frank, which, of course, provided some margin. They had stipulated that the loan should be paid off within two and a half to three years; and in addition to a charge on the dividends they took from the company an agreement until the loan was repaid to pay to the bank all the dividends it received from the shares in reduction of the amount due to the bank from time to time for payment of capital and interest. There was a stipulation that the companies should not during the period of the loan pay directors' fees in excess of £6,000 a year, a provision which suggests that Wilfred was not left without resources. But, as far as the company was concerned, for the time being it placed all its resources of every

kind at the disposal of the bank, and was left without any income of any kind which it could, without the consent of the bank, devote to any purpose. There is no finding that this agreement was made in bad faith, or to avoid super-tax, and the Crown expressly disclaimed any attack upon it as being unreasonable. Indeed, it is easy to see that Wilfred and his wife, as the directors and sole shareholders of the company, might congratulate themselves upon getting an advance from a bank on this class of security of so large an amount with the result that they secured in the near future a very valuable asset at the cost of foregoing for a few years' dividends which so far had amounted to £ 500 or £ 600. The receipts from dividends during the years of charge were £6,540 and £34,855, or, deducting bank interest (in the first year for half a year), £ 5,340 and £ 31,140. The Board of Referees have found that the company had not within a reasonable time distributed in the manner referred to in the section a reasonable part of its income for either period, and restored the direction of the first Special Commissioners that the actual income of the company from all sources should be deemed to be the income of the members and the amount apportioned among them. It is unnecessary to emphasise the highly penal nature of the section. It matters not how small a proportion of the whole income is "the reasonable part" found not to have been distributed. If the company are in fault over a few hundred pounds the shareholders may be credited with many thousands of pounds with correspondingly heavy liabilities for surtax. In the present case the Board of Referees have not found what would have been a reasonable sum to distribute. It is said that they have the support of some decision for this. If it be so I can only say that the decision is wrong in a case stated such as this where the question is, was there evidence to support the decision? I find it impossible to approach the question whether there was evidence to support a finding that "a reasonable part" should be distributed, without knowing what part it was considered reasonable to distribute at least stated as a minimum. In the present case the Solicitor-General stepped into the breach and suggested that at least the company should have distributed £ 500 or £ 600, an amount corresponding to its resources, before it embarked upon the purchase of the operative companies' shares.

The first question stated by the Board refers to a contention that under the agreement with the bank it would have been a breach of contract to distribute a dividend. No such contention was sought to be made by the appellants before this House, and the question becomes irrelevant. The remaining questions are connected and should be set out,

In paragraph 24 of the case the Board of Referees state [his Lordship read the paragraph already set out]. Incidentally it is not to me clear whether this means that the company had failed to produce the kind of evidence referred to, and that if they had produced the evidence they might have displaced the *prima facie* case; or means that there was evidence of the nature referred to, but it did not displace the *prima facie* case. I think it probably means the former.

In paragraph 25 they say [his Lordship read the paragraph]. The two questions now relevant posed by the Board are: "(2) Whether there was evidence to support our finding of fact as set forth in paragraph 25. (3) Whether the matters set forth in paragraph 24 are such as to show that we misdirected ourselves as to the onus of proof in a case where it is admitted that an investment company with a substantial income has not distributed any part of it".

I do not know whether there is any meaning in the inversion of order of the paragraphs in the questions as put. In any case I should conclude that if the Board adopted a view as to the *prima facie* value of certain facts, and the failure of the company to displace those facts, their final decision that the company had not distributed a reasonable part of its income was necessarily based upon their expressed view of the *prima facie* case made and not displaced. On what other footing could the Board have reached a final decision on the facts? It would follow that if they have in fact misdirected themselves in paragraph 24 their finding of fact in paragraph 25 is invalidated by this misdirection.

It seems clear that the discussion must proceed *ab initio* on the footing that the action of the directors must be judged by considering what their conduct would reasonably be if no question of surtax influenced their decision. Withholding of distribution for the purpose of "avoidance of the payment of surtax" by shareholders would, if found, obviously negative the reasonableness of any part so withheld. The other general point to be observed is that, as it seems to me, what has to be found is that the company acted unreasonably in withholding some part of its income from distribution. It is not enough to show that a part could reasonably be distributed, if at the same time it could be said, as it well might, that it was equally reasonable to withhold distribution. The section is highly penal and I feel no doubt that the onus is originally and remains on the Revenue to show that the company acted unreasonably in withholding part of its income from distribution. What is reasonable has consistently been held to depend upon the actual conditions known at the time for decision. In the application of this section it is what *these* directors

recommend and *these* shareholders decide in *those* conditions of *that* company. There is no abstract conception of reasonableness, and the conclusion is not to be reached on *a priori* reasoning. Assuming that the directors are business men, have they acted unreasonably in the circumstances in withholding a distribution? From this point of view I am quite unable to agree that the fact that a company, even an investment company, during the year holds income-producing investments raises a *prima facie* case that the reasonable course for the company is so to manage its affairs as to provide for that income or any part of it to be distributed. It is certainly untrue of private commercial companies of whom I have no doubt numbers are now prospering because the members have year after year placed all their profits in the business, and have foregone any income other than such as they may derive from directors' fees or the like. And I see no reason why the supposed rule should apply to investment companies who are equally entitled if they choose to forego their income for a time to develop and improve the company's undertaking. I think, therefore, that the answer to question three is that the matters referred to do show that the Board misdirected themselves as to the onus of proof.

But I also think that the facts stated by the Board disclose no evidence on which it could be found that the company failed to distribute a reasonable part of its income in the years in question. We may eliminate the question which interested the Court of Appeal whether it was legal for the company, having disposed legally of all its income for the year, to distribute a dividend at all. It was pointed out in the Court of Appeal if the company had made profits it would be perfectly legal to distribute them if it could secure the means to do so out of its other free assets or by borrowing. The point was not argued before us by appellants' counsel in his cogent and convincing address. Whether it would be reasonable to exercise the legal right is another and the only relevant question. It will be convenient here to deal with the argument which was pressed upon us by counsel that in the present case the dividends from the operative companies' shares formed the whole of the "actual" income of the company within the meaning of Section 21 of the Act of 1922, and that as the whole of that "actual" income had been assigned to the bank, there was no part of it which could have been distributed. The Court of Appeal have effectively disposed of this argument. Actual income does not mean the specific receipts that come in from time to time, but the "income-tax income" as calculated at the end of the year of assessment. To hold otherwise would make nonsense of the section when applied to commercial companies, who use their receipts as soon as they come in, and hardly

ever have left for distribution the actual incomings as sought to be defined in the argument.

But when one begins to consider the circumstances of this company at the end of this year when they had to consider the distribution of dividend, I am at a loss to see what was unreasonable in their decision to distribute nothing. There were only two shareholders, in substance only one, Wilfred. They had agreed shortly before by an agreement, which is not now in any way attacked, to assign the whole of their resources to the bank to secure what appeared to be a profitable and reasonable purchase. As a result the company had not any asset left nor any source of free income. They therefore could not procure the funds with which to distribute a dividend without borrowing. They had no source of income from which they could pay interest on any loan. If they had to borrow from some one other than the bank they would have had therefore to pay some capital premium, in lieu of interest calculated for the period of the bank loan; and presumably in the circumstances heavy. It was suggested that they might have approached the bank either for the necessary loan or to release some of the dividends. But the company were represented by the very two people, the only persons interested, who had only a few months before in an agreement which is unassailable agreed to carry out the bank's stipulation that the loan should be paid off in two or three years by surrendering for the time being all the dividends. What is the overwhelming impulse to declare dividends that would now induce them to depart from the bank arrangement, or induce the bank to vary it. In view of these considerations it appears to me that it was for the Inland Revenue authorities to give evidence indicating not only that it was possible for the company to borrow (the Court of Appeal say that it would have been easy to borrow), but that in the circumstances it was the reasonable thing to do. In the result, therefore, I come to the clear conclusion that there was no evidence that the company failed to distribute a reasonable part of its income. I regard the case as turning on the bank agreement. As long as that remains unassailed it must necessarily have controlled the actions of the company and their reasonable decisions. The Court of Appeal spoke of "the whole plan in the present case for protecting its two shareholders from surtax." I cannot reconcile this phrase with their attitude towards the bank agreement; nor do I find it supported by any finding of the Board of Referees.

If the arrangement with the bank was in fact made as part of a plan for avoiding surtax there might very well be evidence of a failure to distribute a reasonable part of the income. But in the absence of any

evidence or finding to that effect and in view of the respondents' disclaimer of any attack on that agreement it must be taken to represent a genuine business arrangement, and is a circumstance of the highest importance in estimating the reasonableness of the company's action.

I am of opinion therefore that the answer to question two should be No and to question three Yes; that the appeal should be allowed and the order of the Court of Appeal should be set aside, and the order of Macnaghten, J., restored; and that the respondents should pay the cost in this House and in the Court of Appeal.

LORD MACMILLAN stated the facts and continued: Two matters dealt with by the Board of Referees have first to be considered. They held (1) that as a matter of construction of the contract with the bank it would not have been a breach of contract for the appellant company to distribute a dividend. That is clearly right. But it is equally clear that it would have been a breach of contract to apply the dividends which the appellant company received and which were its sole source of income to payment of a dividend to its own shareholders. Therefore if the appellant company was to pay a dividend it must find the money from some other source than the dividends which it had itself received. The only possible source suggested by the Inland Revenue is that "if necessary the company could lawfully have borrowed the necessary money to enable it to make such distribution." But in the stated case the Board do not find in fact that the company could have borrowed the necessary money or that it would in the circumstances have been reasonable for the company to do so. Then (2) the Board found as a fact that, if they were wrong in holding that the company without breach of contract could have declared a dividend, "it was not reasonable for the company to make such a contract." At your Lordships' bar, however, the Solicitor-General for the Crown expressly disclaimed any attack on the appellant company's contract with the bank as being in itself unreasonable. I think this concession was rightly made for, considered apart from any question of taxation, the contract appears quite unobjectionable.

Once it is conceded that the contract is not assailable as unreasonable and consequently that it was not unreasonable for the appellant company to contract to pay over its whole income to the bank, it becomes difficult to see how it can be said to have been unreasonable to refrain from distributing dividends which could have been provided only out of borrowed money. No indication is given of any grounds on which it would have been reasonable for the company to borrow money to enable it to pay a dividend. If a dividend had been paid it

would not in fact have been paid out of profits, but out of borrowed money. It would not have been a distribution of profits but a distribution of borrowed money which it was legitimate to distribute because a corresponding amount of profits had been earned.

What, then, is the finding in fact by the Board which your Lordships are asked to hold as justifying the Board's conclusion that the appellant company had not distributed in dividends a reasonable part of its income? It is to be found in paragraph 24 of the stated case, which expresses the opinion of the Board [his Lordship read paragraph 24]. The reference to the figure of £ 18,000 relates to the purchase price of the shares which the appellant company purchased from its own resources as distinct from the money borrowed from the bank.

It will be observed that the paragraph I have quoted puts the matter as one of onus. It may well be that when the Special Commissioners make a direction under Section 21 of the 1922 Act it is for the company to put forward reasons and if necessary evidence to show why the direction is in the circumstances unjustified. Here the appellant put forward their contract with the bank as justifying their having made no distribution of their income in dividends. And the Crown admit that it was quite reasonable for the company to contract to apply its income as it did. It seems to me that it was then for the Crown to show that it would have been reasonable for the company, notwithstanding its contract with the bank, to raise money by borrowing or otherwise in order to pay a dividend, as there was no legal obstacle to its doing so, and that the company could in fact have raised the necessary money. There is no trace of any such evidence in the case. But when the matter reaches the stage of a stated case, the question is not properly one of onus. It is simply a question of whether the facts found and stated afford evidence on which the Board could properly arrive at their conclusion. Now all that paragraph 24 of the stated case finds is that *prima facie* the reasonable course was that the company should so manage its affairs as to provide for distribution of dividend. This is rather an expression of opinion than a statement of fact, and no grounds are given for it. The result is that in my opinion the Board have not stated any facts such as to justify them in holding that the appellant company failed to distribute a reasonable part of its actual income in the years in question. I am accordingly in agreement with all your Lordships that the appeal should be allowed.

LORD WRIGHT.—I have considered in print the speech which my noble and learned friend the Lord Chancellor has delivered. I agree

with it and merely add a few words as your Lordships are differing from the Court of Appeal.

The Board of Referees have embodied their decision in a case stated for the opinion of the Court and have made it for present purposes subject to two questions of law. I disregard the first question which is now irrelevant. As to the second question which is whether there was evidence to support the Board's finding that the company had not within a reasonable time distributed a reasonable part of its income for the periods in question, that is a question of law which depends on an analysis of the facts found in the special case. But I think it cannot properly be disposed of without considering the other question which is logically prior though postponed in the order in which the case is stated. That latter is in truth a question as to the onus of proof, and can only be understood by referring to paragraph 24 of the case. I understand that paragraph to mean that the Board are treating the onus as of an ambulatory or shifting character, so that at a certain stage of the inquiry it finally shifts from the respondent to the appellant. I think that is wrong in law. The Crown set out to prove that the direction of the Board is justified because the appellant company has not distributed a reasonable part of its income within the meaning of Section 21 of the Finance Act, 1927. It is obvious that the section is penal in character, and in my opinion the onus is finally on the Crown to prove its right to impose what is a very severe penalty. At the end of the day it is for the Crown to establish the facts necessary to show want of reasonableness on the part of the appellant. I cannot discover in the case as stated that there are facts found sufficient to justify the conclusion. Nor do I think that the Board would have come to their conclusion if they had not taken the view as to onus expressed in paragraph 24. It was for the Crown to establish that the appellant company could have produced funds (it being accepted that the contract with the bank was not unreasonable) out of which to declare a dividend "without jeopardising the interests of the company or without making it impossible to acquire the shares which it desired to buy." I accept this here as a correct statement of what would have been sufficient if established. The Board have not found that this has been proved. It seems to me that their conclusion in paragraph 25 was based upon their view as to the onus of proof. If the Board were wrong in that view, and I think they were, it follows that in law there was no evidence to support their finding of fact in paragraph 25.

LORD PORTER.—I agree that this appeal should be allowed, and I think I can state with brevity my reasons for coming to this conclusion.

The facts have already been fully set out from the Woolsack, including in particular paragraphs 23, 24 and 25 containing the findings of the Board of Referees from which as I understand it that body draws its inferences and conclusion. The case ends by asking certain questions for the opinion of the Court, questions which as a result of the present appeal it is now incumbent upon your Lordships to answer.

As regards the first, I agree with the Lord Chancellor in thinking that it would not have been a breach of contract for the company to distribute a dividend despite the fact that it had already assigned all its income to the bank in order to repay the loan obtained, and had also hypothecated the whole of its assets for that purpose. Reference has already been made to the *Montague Burton Case*¹, which establishes this proposition. In view of this opinion the alternative suggestion that it was not reasonable for the company to make such a contract becomes immaterial, but I should not consider it material in any case. A company is entitled to manage its own business in its own way; the question for the Board of Referees is not, as I see it, whether the company has taken a reasonable course, but whether, the particular course having been taken, the company has distributed a reasonable part of its actual income. In saying this I do not rule out the possibility that it may be seen in a particular instance that no genuine transaction has taken place and that the bargain made, actual or purported, is really a subterfuge merely adopted to avoid the payment of tax. I am not saying that such a state of affairs should not be taken into consideration in determining whether a reasonable part of a company's income has or has not been distributed. Moreover, I agree with the noble Viscount and with the Board that the decision in the *Glased Kid Case*² is open to the objection that it appears to assume that a dividend, at any rate in the case of a holding company, can only be paid out of income received or receivable as cash. The fact that the income had been invested or hypothecated for some purpose elsewhere would not of itself necessarily prevent the distribution of a dividend.

Subject to the qualification that the opinion of the Board of Referees as to the reasonableness of the contract entered into is in this case an immaterial consideration, I should answer the first question asked by the case in the affirmative.

There is, however, as I think, more difficulty in answering the second question. As I understand the framework of the case the deductions and inferences drawn by the Board from the history of the transactions set out in the earlier paragraphs are brought to a conclusion in paragraph 24, and therein are to be found the grounds from which it is determined that a reasonable distribution of income had not been made.

(1) (1936) 20 Tax Cas. 48; 4 I.T.R. Suppl. 12.

(2) (1930) 15 Tax Cas. 445.

Those reasons are, I think, as follows : (1) The company is an investment company ; (2) it held income-producing investments which cost £18,000 ; (3) having those investments it should have managed its business in such a way as to insure that the company enjoyed the income produced by them either directly or indirectly ; (4) the company had not proved that it could not have kept this income without endangering its interests and without preventing itself from purchasing the shares acquired by means of the loans from the bank.

(1) The company is indeed an investment company, and I suppose it is possible to say that in such a case the necessity for building up considerable reserves may not be so imperative as in the case of a trading company—at any rate the Board was entitled to think so, even in the case of a company holding somewhat speculative shares. But this circumstance seems to have little bearing upon a case where the putting by of reserves does not come in issue, but only the making of a speculative but profitable investment. (2) and (3). Nor does it seem to me of much assistance to say that the company once held and, subject to the bank's interest, still holds investments costing £18,000. The question is what distributable revenue those investments do or ought to produce. The statement in its bald form appears only to be another way of saying that the purchase of the additional shares ought either not to have been made at all or, at any rate, ought not to have taken the form it did, and seems to merge in allegation (4), namely, that it had not been proved impossible to acquire those shares in some other way. (4) To say that it would have been possible to raise the loan required on less onerous terms without any suggestion as to how it could have been done or whence the money could have been obtained is indeed to enter the realm of conjecture. In fact, the money was raised by loan from the bank, and in fact the bank insisted upon the terms agreed ; indeed, so far as the evidence is concerned it was anxious to have the total sum repaid at an earlier date than that finally stipulated.

If, then, positive evidence is required to support the finding in paragraph 25 of the special case that the company had not distributed a reasonable portion of its income, I can find none. So far as the bank is concerned it is negatived, and so far as any other source is concerned it is merely conjecture. Indeed, as I think, paragraph 24 depends, and having regard to the form of the case stated depends solely, upon the assumption that the onus of proof is on the company to show not that it could have raised money to pay a dividend after making the bargain into which it had entered, but that it could have made a better bargain. If the finding in the case had been that the appellants could and should reasonably have raised money or credit

upon the equity of redemption of the assets pledged to the bank, and so could have provided funds sufficient to declare a dividend, or even that it would have been reasonable to raise the money in this way and the appellants had not shown they could not do so, I should have hesitated in differing from the Court of Appeal.

But that is not how I understand the Board to have reached the result arrived at. It is the bargain with the bank of which they complain, not the failure of the company, once that bargain was made, to obtain such funds as would enable it to distribute a dividend.

If the contract with the bank had not been, as it obviously was, a genuine transaction, but only a matter of avoiding tax, or if it had been found that the directors of the company could, and as reasonable business persons should, have borrowed on the security of their equity of redemption, or even that, as reasonable business persons, they should have done so if they could, and it had not been shown that they could not, I should be unwilling to vote for allowing the appeal. But there is no such finding and I do not think that the respondents' case is strengthened by a suggestion that quite a small sum should have been raised for the purpose. The question is what should reasonably have been done. If it was possible and reasonable for the appellants to borrow at all in the present case, I think the facts found would support the inference that a considerable sum could have been borrowed just as readily as they would support the inference that a small one should have been borrowed. But I do not think they support either. The appellant's duty is to act reasonably, not to adopt any and every means in order to scrape up enough money to declare a dividend, however small.

It will be seen that the opinion which I have expressed is based upon the exact findings of the Board of Referees as I understand those findings. May I add that it would assist a tribunal, to which a case stated is referred, if the facts found were carefully separated from the inferences of fact and law based upon them, and if those inferences themselves were clearly distinguished.

In *Bomford v. Osborne* (also a tax case) 110 L.J.K.B., at p. 479; [1942] A.C., at p. 46, I expressed the view that in setting out a case it was not legitimate, after stating the facts, to reach a certain conclusion by saying that such and such a thing is found as a fact. I am still of this opinion, and think that the final conclusion is not a fact but an inference from facts previously set out, and that therefore that conclusion is not binding upon the tribunal to which the case is referred unless it appears from the previous findings that there are facts which support it. In the present case I cannot find such support and should allow the appeal.

Appeal allowed.

[IN THE HOUSE OF LORDS.]

TILLEY v. WALES (INSPECTOR OF TAXES).

THE LORD CHANCELLOR (VISCOUNT SIMON), LORD ATKIN,
LORD THANKERTON, LORD RUSSELL OF KILLOWEN, LORD PORTER.

Dec. 10, 11, 14, 1943; Feb. 11, 1943.

INCOME TAX—DIRECTOR OF COMPANY—AGREEMENT FOR SALARY AND PENSION—SUBSEQUENT AGREEMENT TO COMMUTE RIGHTS BY LUMP SUM IN TWO INSTALMENTS—WHETHER LUMP SUM TAXABLE AS INCOME—SO MUCH OF SUM REPRESENTING LOSS OF SALARY TAXABLE—PART APPORTIONED TO RELEASE OF PENSION NOT TAXABLE—ENGLISH INCOME TAX ACT, 1918 (8 & 9 GEO. 5, c. 40), SCHED E.

A limited company agreed to pay the appellant £6,000 a year for acting as managing director, and in the event of his ceasing from any cause to be managing director a yearly pension of £4,000 for ten years. By a subsequent agreement, the appellant released the company from its obligation to pay him the pension and agreed to accept a salary of £2,000 a year in consideration of the company's undertaking to pay him £40,000 in two instalments of £20,000 each:—Held, (1) that neither the pension nor the sum paid to commute it constituted profit of an office within the meaning of rule 1 of Schedule E to the Income-tax Act, 1918. The ratio decidendi of the House in DEWHURST v. HUNTER [1932] (146 L. T. 510; 16 Tax Cas. 605) applied. (2) Whatever part of the £40,000 should be regarded as the equivalent of a drop in salary amounting to £4,000 a year, was within the charge on profits from the office of director in Schedule E: CAMERON v. PRENDERGAST [1940] (8 I.T.R. Supp. 75; [1940] A. C. 549) applied. (3) The Attorney-General having agreed before the House that, having regard to the above two decisions, the two sums of £20,000 each should be treated as apportionable, those two assessments should be referred back to the Commissioners to determine what would be a reasonable apportionment.

Decision of the COURT OF APPEAL (111 L.J.K.B. 558; [1942] 2 K.B. 169) reversed in part and in part affirmed.

Cases referred to;

Cameron v. Prendergast (1940) 109 L.J.K.B. 486; (1940) A. C. 549; (1940) 8 I.T.R. Supp. 75.

Dewhurst v. Hunter (1932) 146 L.T. 510; 16 Tax Cas. 605.

Short Bros., Ltd. v. Inland Revenue Commissioners (1927) 136 L.T. 689; 12 Tax Cas. 955.

Appeal from the judgment of the Court of Appeal.

The facts are fully stated at the commencement of the Lord Chancellor's judgment.

Needham, K. C., and Donovan, for the appellant.

The Attorney-General (Sir Donald Somervell, K. C.), and Reginald P. Hills, for the respondent Inspector of Taxes.

Their Lordships took time for consideration.

THE LORD CHANCELLOR.—The question in this case is whether two sums of £20,000 each which were paid to the appellant by a company named Stevenson & Howell, Ltd., carrying on the business of manufacturing chemists, of which he was managing director, fall to be assessed for income-tax under Schedule E as being profits from his employment as such director. The circumstances in which this question arises are very special, and before a correct solution can be reached it is necessary to refer to three agreements made at different dates between the company and the appellant.

The first of these agreements is dated December 19, 1921. It recites that the appellant was the inventor of a secret process for the manufacture of a product to be used by the company in connection with their business. Under this agreement the appellant, who was already a director of the company, divulged to the then managing director his secret process, and the company contracted to pay to the appellant a royalty of one shilling upon every pound weight of the new product manufactured under the secret process and used by the company.

The next agreement to be referred to is dated June 28, 1937. By that time Mr. Tilley had become managing director and was receiving a salary as such of £2,000 per annum. The agreement cancelled the arrangement of 1921 for the payment of the royalty, and in consideration of this provided that the appellant's salary as managing director should be raised to £6,000 per annum, and that, in the event of the appellant ceasing from any cause whatsoever to be managing director of the company, the company would pay to him from the date of cessation a pension of £4,000 per annum for ten years from such date. As long as matters stood on the basis of the 1937 agreement, there can be no doubt that the appellant's salary of £6,000 per annum was subject to income-tax under Schedule E and that, when his service as managing director ceased, the pension of £4,000 per annum was equally liable to tax under the second limb of that schedule. The agreement of 1937 ended with a paragraph providing that the expression "Mr. Tilley" includes, where the context so permits, his personal representatives. As the Court of Appeal has pointed out, this makes the construction of the agreement, so far as it provides for "pension", somewhat difficult, and in view of the nature of the conclusion at which

I would invite the House to arrive, it is desirable to indicate whether under the agreement the pension would in any case cease with the appellant's death or whether it would be payable, in the event of his death, to his personal representatives until the period of ten years had elapsed. I think the second of these constructions is the correct one.

Lastly, there comes the agreement dated April 6, 1938. It recites the provisions made the year before for a salary of £ 6,000 per annum as managing director and for a pension of £ 4,000 per annum for ten years on the appellant ceasing to be managing director. The agreement then goes on to record that the company has requested the appellant (1) to release it from the prospective obligation to pay the pension, and (2) to serve the company in future at a salary of £ 2,000 per annum. The agreement witnesses the appellant's acceptance of these requests, and in consideration of this "the company will pay to Mr. Tilley the sum of £ 40,000 by two equal instalments, the first of which shall be paid on April 6, 1938, and the second on April 6, 1939".

It is evident, therefore, that the £ 40,000 on which the Crown seeks to levy income-tax is paid in part as the price of compounding the pension, and in part in consideration of the reduction of the appellant's annual salary from £ 6,000 to £ 2,000. I will postpone the consideration of any difficulty which might arise from the fact that the total of £ 40,000 is stated as a single sum and is not divided by the terms of the agreement into two parts allocated respectively to the compounding of the pension and the reduction of salary, and will first consider how far Schedule E would be applicable if the two matters were dealt with separately, £X being stated in the agreement as representing the value of the pension rights, and £Y as being paid in return for the reduction of salary, so that the two sums added together, £X plus £Y, amounted to the total of £ 40,000.

If it is legitimate to separate out the consideration in this way, it appears to me that there are two decisions of your Lordships' House which guide us to the conclusion at which we must arrive, one in connection with the pension problem and the other in connection with the payment in respect of the reduction of salary. As regards the commutation of pension, I cannot agree with Lawrence, J.'s view that, as the pension would have been assessable under Schedule E, therefore a sum payable in commutation of it would also be assessable under the same schedule. I think that the Master of the Rolls is right when he says that the decision in *Short Bros., Ltd. v. Inland Revenue Commissioners*¹ to which Lawrence, J., referred in this connection, does not support

(1) (1927) 136 L.T. 689; 12 Tax Cas. 955.

the learned Judge's proposition, and neither can I accept the contention contained in the case for the respondent (but not, as I understood, persisted in by the Attorney-General) that the pension under the agreement of 1937 was deferred remuneration and that the acceptance by the appellant during his service of a sum in commutation of the pension amounted to the acceptance of a present remuneration instead. Neither the pension, nor the sum paid to commute it constituted, in my opinion, profit from the office. If pension was paid after ceasing to hold the office, it would have been assessable under the head of "pension" in Schedule E and the First Rule applicable to that schedule. I agree with the unanimous view of the members of the Court of Appeal that a pension is in itself a taxable subject-matter distinct from the profit of an office, and if an individual agrees to exchange his right to a pension for a lump sum, that sum is not taxable under Schedule E. This conclusion is in accordance with the views of the majority of the Law Lords when this House decided the case of *Dewhurst v. Hunter*.¹ There an article of association of the company which had employed Commander Dewhurst provided that when a director died or resigned or ceased to hold his office for a cause not reflecting upon his conduct or competence, the company should pay to him or his representatives by "way of compensation for the loss of office" a sum equal to the total amount of his remuneration in the preceding five years. Commander Dewhurst subsequently agreed with the company, at a time when he was ceasing to be chairman but was remaining a director, that in lieu of his rights under this article he should be paid £10,000, while his remuneration as director was at the same time reduced to £250 per annum. Lord Warrington, Lord Atkin and Lord Thankerton held that the £10,000 was not a profit from his employment as director and did not represent salary, but was a sum of money paid down by the company to obtain a release from a contingent liability as distinguished from being remuneration under the contract of employment. Lord Thankerton emphasised the further point that the payment was not in the nature of income at all. It is true that the decision in *Dewhurst's Case*¹ was regarded and described as arising under very special circumstances, but I think the *ratio decidendi* is as I have described. Moreover, apart from previous authority, I should myself take the view that a lump sum paid to commute a pension is in the nature of a capital payment which is substituted for a series of recurrent and periodic sums which partake of the nature of income.

But can the same view be taken of an arrangement made between an employer and his servant under which, instead of the whole or part

(1) (1932) 146 L.T. 510; 16 Tax Cas. 605.

of a periodic salary, a single amount is paid and received in respect of the employment? Generally speaking, I think not. An "office or employment of profit"—to use the actual phrase in Schedule E—necessarily involves service over a period of time during which the office is held or the employment continues. The ordinary way of remunerating the holder or the person employed is to make payments to him periodically, but I cannot think that such payments can escape the quality of income which is necessary to attract income-tax because an arrangement is made to reduce for the future the annual payments while paying a lump sum down to represent the difference. My view seems to me to be supported by the decision of this House in *Cameron v. Prendergast*.¹ In that case the respondent was a director of a company and was minded to resign his position and so obtain greater ease. His fellow directors, in the interests of the company's success, urged him not to do so, and an agreement was made between the company and himself under which his salary was reduced from £ 1,500 to £ 400 per annum, but he also received £45,000. This House decided that the £45,000 was a profit from the respondent's directorship and was therefore assessable under Schedule E. I am not myself prepared to go so far as to say, as was said by the Master of the Rolls and Goddard, L.J., in the present case, that remuneration for service can never be capital in the sense which would put it outside income-tax. It is worth pointing out that the word "remuneration" does not occur in Schedule E at all and it is safer to use the words of the statute. I prefer to limit myself to the case now under consideration, and to say that, whatever part of the £ 40,000 should be regarded as the equivalent of a drop in salary amounting to £4,000 a year, is within the charge on profits from the office of director.

There remains the question, which might otherwise have raised some difficulty, whether, when capitalisation of pension is not taxable and a sum paid in compromise of a reduction in salary is taxable, the £ 40,000 which is agreed between the parties to be the value of the two things together can be split up. We are relieved in the present case from deciding the point, for the Attorney-General agreed that the two sums of £20,000 each should be treated as apportionable if the House took the view that tax was due under one head but not under the other. Accordingly I move that these two assessments should be referred back to the Commissioners in order that they may determine, according to the best of their judgment, what would be a reasonable apportionment. So much of the two sums as should be taken as paid in substitution for the reduction of salary should be assessed, in the appropriate

(1) (1940) 109 L.J.K.B. 486; (1940) A.C. 549; 8 L.T.R. Supp. 75.

years, for tax under Schedule E. The balance of the two sums which should be regarded as representing the purchase price of the annuity should escape taxation. I move accordingly. The appellant should have his costs of the appeal to this House, and there should be no costs in the Court of Appeal on either side.

THE LORD CHANCELLOR.—My Lords, I am authorised by my noble and learned friends Lord Atkin and Lord Russell of Killowen to say that they concur in the opinion which I have just delivered.

LORD THANKERTON.—The Crown claims that the sum of £40,000 paid to the appellant in two instalments at a year's interval under the agreement of April 6, 1938, is chargeable to income-tax under Schedule E of the Income Tax Act of 1918, as paid to him in respect of his office of director and coming within the words of rule 1 of Schedule E, namely, "all salaries, fees, wages, perquisites or profits whatsoever therefrom".

My noble and learned friend on the Woolsack has made sufficient reference to the various agreements, and I agree that in order to appreciate the two-fold consideration in return for which the £40,000 was agreed to be paid, it is necessary to refer to the agreement of June 28, 1937, the terms of which equally necessitate a reference to the earlier agreement of December 19, 1921. The Crown failed before the Special Commissioners, on the ground that the payment of £40,000 was not made to the present appellant as remuneration for services rendered or to be rendered to him in his office as a managing director of the company. On appeal, by stated case, Lawrence, J., decided in favour of the Crown, holding that both in form and substance the payment was made in consideration both of the release from the company's obligation to pay the pension and the present appellant's agreement to serve at a reduced salary of £2,000 per annum. As regards the latter element, the learned Judge held that it was clearly a profit from the office, and, as regards the ten-year pension, he held that, as the pension would have been assessable under Schedule E by virtue of Section 17 of the Finance Act, 1932, the sum payable in commutation thereof was assessable under Schedule E, and he based this finding on the decision in *Short Brothers, Ltd. v. Inland Revenue Commissioners*.¹

An appeal by the present appellant to the Court of Appeal was dismissed, but partly on grounds materially different from those of Lawrence, J. All the learned Judges differed from his statement as to the assessability of a sum paid in commutation of a pension and the Master of the Rolls pointed out that the case of *Short Brothers*¹ did

(1) (1937) 136 L.T. 689; 12 Tax Cas. 255.

not support the view of the learned Judge; further, all the learned Judges of the Court of Appeal were of opinion that, if the agreement of 1938 had expressly apportioned the consideration of £ 40,000 between clauses 1 and 2, the portion referable to clause 1, which released the pension obligation, would not have been chargeable to tax, but that the portion referable to clause 2, which contained the agreement to serve as managing director at a reduced salary, was chargeable to tax, as it fell directly within the decision of this house in *Cameron v. Prendergast*.¹ But the learned Judges—MacKinnon, L.J., *dub.*—held that, as the parties themselves had refrained from apportionment, an apportionment by the Court was not permissible. Goddard, L.J., appears to have further held that, in view of the conditions attached to the payment of the pension, it would be impracticable to make such an apportionment.

In common with all the learned Judges below, I have no doubt that in so far as the payment of the £ 40,000 may be referable to the agreement to serve as managing director at a reduced salary, there is liability to tax, the decision in *Prendergast's Case*¹ being directly in point. It satisfies, in my opinion, the two tests, namely, (i) whether it arose from the office of director within the meaning of rule 1, and (ii) whether it is in the nature of income. I may add that I doubt whether the word "capital" is the exact antonym to the later test. While I would agree that according to common experience, any consideration given in return for services in the office of director is likely to be in the nature of income, I am not prepared to state dogmatically that it must in every conceivable case be so, whatever form it takes, as the learned Master of the Rolls and Goddard, L. J., appear to think. It is enough that there is no difficulty in the present case.

In so far as the payment of the £ 40,000 may be referable to the agreement to accept a sum in commutation of the liability to pay a pension, I have nothing to add to the view expressed by my noble and learned friend on the Woolsack. As in *Dewhurst's Case*², such payment did not arise from the office of director, but in spite of it. I also agree with the view expressed by my noble and learned friend on the question of apportionment. I would desire to note, on the question of practicability, referred to by Goddard, L. J., that the present appellant's accountants appear to have provided the basis for the agreed sum of £ 40,000, as stated in paragraph 8 of the stated case. I concur in the motion proposed by my noble and learned friend.

LORD PORTER.—As MacKinnon, L.J., has pointed out, your Lordships are not without assistance when considering the problem which

(1) (1940) 109 L.J.K.B. 486 ; 1940 A.C. 549. (2) (1932) 146 L. T. 510 ; 16 Tax Cas. 605.

this matter presents. In *Dewhurst v. Hunter*¹ and *Cameron v. Prendergast*², this House had at least discussed the question and in my view has decided it.

By the so-called "1938" agreement the appellant received two sums of £20,000 each and in return gave two separate considerations: (i) He released the company from an obligation to pay a pension of £4,000 a year for ten years from his ceasing to be managing director; and (ii) he agreed to serve the company at a reduced salary of £2,000 (instead of as theretofore at £6,000 granted him by the 1937 agreement.)

It was claimed for the Crown that both these two sums of £20,000 were taxable as a profit from the directorship, but that even if the former was not so taxable the commutating sums paid for each were so inextricably interwoven that it was not possible to ascertain how much was paid for the one and how much for the other, and that consequently the subject must pay on the whole. This was, as I understand it, the view of the majority of the Court of Appeal. MacKinnon, L.J., however, though he would himself have taken the view that each item would be severally taxable, held himself bound by the principles evolved in the two cases referred to above and therefore considered that any sum paid in commutation of the pension was not taxable, whereas the sum paid as a consideration for the agreement to serve on as managing director at a reduced salary was taxable. I agree that this result follows if the remuneration can be apportioned between salary and pension. As I see it, your Lordships have so decided in the cases referred to above and are bound by authority so to hold.

The Attorney-General argued that this present case differed from *Dewhurst v. Hunter*¹ in that the sum paid in commutation of the pension rights was paid whilst the appellant was still serving as a director and that the sum paid in commutation of a pension to a person so serving differed from that paid in respect of a pension already due to a director whose service had come to an end. I do not feel able to accede to this argument. In my view a sum received upon the sale or surrender of pension rights is not taxable under Schedule E, because it is neither pension nor annuity and comes under no other heading of that section. It is in the headnotes to *Dewhurst's Case*¹ said to be exempt as being capital and not income. It is not, as I think, a pension or annuity; and therefore not income taxable under Schedule E, but I doubt if much assistance is to be obtained by making use of the antinomy between capital and income. The Attorney-General sought to distinguish *Dewhurst v. Hunter*¹ on the ground that in that case the pension was not deferred pay whereas in this case it was, and admitted that if

(1) (1932) 146 L.T. 510; 16 Tax Cas. 605. (2) (1940) 8 I.T.R. Supp. 75; (1940) A.C. 549.

it were not the Crown would have no claim to tax. Such a contention makes it necessary to determine the grounds upon which the pension was granted in the 1937 agreement. No special consideration is stated in that document: the granting of the pension apparently forms one of the general terms of the agreement under which the appellant promises to give up his right to receive one shilling in respect of each pound of material manufactured under his secret process. Moreover, the pension is payable at any moment at which he may cease to be employed as managing director whatever the cause, and it is apparently payable to his personal representatives. I cannot think that such a provision represents deferred pay. It looks much more like a payment in lieu of the stipulated reward for revealing the secret process. But it is unnecessary to speculate. It is a sum paid for the release of an obligation to provide a pension and not shown to be given instead of deferred pay. If so, it is admittedly not subject to tax. Just as in my opinion it follows, from the reasoning in *Dewhurst's Case*¹, that any part of the two sums of £20,000 which was paid in respect of the surrender of the pension rights is not subject to tax under Schedule E, so in consequence of the decision in the *Prendergast Case*² the remaining part of the sum which was given in lieu of the surrendered payment of £4,000 as managing director is, I think, taxable as a profit from a public office.

It only remains, therefore, to see whether the sum attributable to the release of the pension can be separated from that payable for the reduction of salary. It was only faintly argued on behalf of the Crown that such a division was not possible; but it was said that there were no materials upon which such a calculation could be made, inasmuch as the cessation of the salary and the commencement of the pension were dependent on many unascertainable matters, amongst others on the appellant's choice of the time of his retirement. No doubt there are difficulties, but the resultant figure seems no more incalculable than, say, the length of time during which an injured workman would have continued to earn wages had he not received his injury, a period difficult no doubt to ascertain, but one which has constantly to be estimated in dealing with cases of personal injury.

I agree that this appeal should be allowed in part and in part dismissed, and concur in the order suggested by the Lord Chancellor.

Appeal allowed in part and in part dismissed.

(1) (1932) 146 L. T. 510; 16 Tax Cas. 605. (2) (1940) 8 I.T.R. Suppl. 75; (1940) A.C. 549.

[IN THE HOUSE OF LORDS.]

LATILLA v. INLAND REVENUE COMMISSIONERS.

THE LORD CHANCELLOR (VISCOUNT SIMON), LORD ATKIN,
LORD THANKERTON, LORD RUSSELL OF KILLOWEN,
LORD PORTER.

Dec. 8, 9, 10, 1942; Feb. 11, 1943.

INCOME TAX AND SUBTAX—ASSETS TRANSFERRED TO RHODESIAN COMPANY—NON-INTEREST DEBENTURES GIVEN AS CONSIDERATION—GRADUAL REDEMPTION OF DEBENTURES—MONEY RECEIVED BY RESIDENTS IN UNITED KINGDOM—LIABILITY TO INCOME TAX AS “INCOME PAYABLE” BY VIRTUE OF TRANSFER—FINANCE ACT, 1936 (26 GEO. 5 & 1 EDW. 8, c. 34), s. 18*—FINANCE ACT, 1938 (1 & 2 GEO. 6, c. 46), s. 28 (2).

Partners holding two one-third shares in a Rhodesian mine in 1933 transferred their interests to a Rhodesian company which continued to carry on the business in partnership with M., the third partner. The company, in consideration of the transfer of the partnership assets, allotted the retiring partners ordinary shares and non-interest bearing debentures in the company, which made substantial profits. Such profits were not distributed as dividends, but each year money was taken out of the profits for the redemption of debentures and for loans to the debenture holders: Held, that by receiving sums in redemption of the debentures there was “power to enjoy” income of the Rhodesian company within the meaning of section 18 (3) of the Finance Act, 1936, and the right by virtue of which there was such “power to enjoy” had been acquired by means of the sort of transfer to which section 18 applied. Trade profits made by a partnership could be said to be income a share of which “becomes payable” to one of the partners. The company was entitled to call upon its partner to do whatever might be necessary, for example, by signing a cheque on the banking account of the partnership, to enable the company to obtain its share, and in the partnership accounts the company’s undrawn share of profits would appear as a debt owing to the company. Therefore it was income “payable” to the company, and was taxable under the Act. The recent case of CITY OF LONDON INCOME TAX COMMISSIONERS v. GIBBS [1942] (111 L. J. K. B. 301; [1942] A. C. 402; 10 I.T.R. Suppl. 121) showed that the technical view of the nature of partnership in English law cannot always be taken in applying the law of income-tax.*

Decision of the COURT OF APPEAL (111 L. J. K. B. 161; [1942] 1 K. B. 299; 10 I.T.R. Suppl. 74) affirmed.

* This section corresponds to Sec. 44-D of the Indian Income-tax Act.—Ed.

Cases referred to :—

City of London Income Tax Commissioners v. Gibbs [1942] (111 L. J. K. B. 301 ; [1942] A. C. 402 ; 10 I.T.R. Suppl. 121.

Psalms and Hymns (Trustees of) v. Whitwell [1890] (7 T. L. R. 164 ; 3 Tax Cas. 7).

R. v. Special Income Tax Commissioners ; Shaftesbury Homes and Arethusa Training Ship, *Ex parte* [1922] (92 L. J. K. B. 152 ; [1923] 1 K. B. 393).

Appeal from the judgment of the Court of Appeal.

The facts are fully stated in the judgment of the Lord Chancellor.

Tucker, K. C., and *Terence Donovan*, for the appellant.

The Attorney-General (Sir Donald Somervell, K.C.), *J. H. Stamp*, and *R. P. Hills*, for the respondent Commissioners.

Their Lordships took time for consideration.

THE LORD CHANCELLOR.—Of recent years much ingenuity has been expended in certain quarters in attempting to devise methods of disposition of income by which those who were prepared to adopt them might enjoy the benefits of residence in this country while receiving the equivalent of such income, without sharing in the appropriate burden of British taxation. Judicial *dicta* may be cited which point out that, however elaborate and artificial such methods may be, those who adopt them are “entitled” to do so. There is, of course, no doubt that they are within their legal rights, but that is no reason why their efforts, or those of the professional gentlemen who assist them in the matter, should be regarded as a commendable exercise of ingenuity or as a discharge of the duties of good citizenship. On the contrary one result of such methods, if they succeed, is of course to increase *pro tanto* the load of tax on the shoulders of the great body of good citizens who do not desire, or do not know how, to adopt these manoeuvres. Another consequence is that the Legislature has made amendments to our income-tax code which aim at nullifying the effectiveness of such schemes. The question in the present appeal is whether Section 18 of the Finance Act, 1936, has the result of checkmating the design of avoiding income-tax and surtax which was the main purpose of certain highly artificial dispositions made in 1933. The appellant contended before the Special Commissioners, before Lawrence, J., and before the Court of Appeal that the avoidance of British taxation was not the main purpose of these arrangements. He failed in this contention at each stage. One of the reasons adduced in his printed case to this House is that the scheme adopted in 1933 “was a *bona fide* commercial operation not designed for the purpose of such avoidance.” If this were true, the scheme would have come within the exemption provided, as the law then stood, for operations not effected for the main purpose of avoiding liability to taxation, and the appellant would escape tax. His counsel prudently decided to drop the contention. The

contrary finding adopted by the Special Commissioners and affirmed by both Courts below, is, as the Master of the Rolls says, "quite unassailable." Nevertheless, if the Crown is unable to bring the scheme of 1933 within the range covered by Section 18 of the Finance Act, 1936, the appellant must succeed. The issue turns on a comparison of the particular arrangements now before us and of the language of the section.

The arrangements, so far as relevant, can be summarised as follows. There existed in Rhodesia a partnership firm called John Mack & Co., which owned and worked an enterprise known as the Golden Valley Mine. Mr. Mack, who lived in Rhodesia, owned a one-third share. Four ladies, namely, the appellant's wife, her two daughters, and Mrs. Jane Johnson, owned the rest. On March 20, 1933, by an agreement of that date, these four ladies, being all at that time resident in the United Kingdom, sold as from April 1, 1932, their shares in the partnership to a limited company formed for the purpose and registered on the same date under the laws of Southern Rhodesia. The company was named the Latjohn Trust, Ltd. The consideration was £260,000, satisfied by the issue to the sellers of ten thousand £1 shares, and 250,000 debentures of £1 each. The debentures carried no interest, and there was no provision as to period of redemption. It is manifest that they were brought into existence merely in order that their redemption might serve as a means, from time to time, of transferring part of the profit of the mine to these ladies in the form of capital. The appellant's wife was entitled to one-sixth of the consideration, namely, 1,667 shares and 41,667 debentures. Latjohn Trust, Ltd., proceeded to carry on business in partnership with Mr. Mack, and the accounts show the sums receivable by the company in the various years in respect of its two-third share of the profits of John Mack & Co. Latjohn Trust Ltd., has never declared a dividend, but has applied its profits in redeeming debentures. It has been the practice of the four ladies to borrow money from the company in anticipation of the redemption of debentures which they held.

Until the Finance Act, 1936, came into force, Mrs. Latilla, as the result of these arrangements, was able to obtain for herself a share in the profits which the Latjohn Trust, Ltd., derived from the partnership business, without incurring for herself or for her husband, the appellant, any liability to British income-tax. Admittedly, by receiving sums in redemption of her debentures, she has "power to enjoy" income of Latjohn Trust, Ltd. (see sub-section (3) of Section 18 of the Finance Act, 1936). The decisive question is whether the right by virtue of which she has this power to enjoy has been acquired by means of the sort of transfer to which Section 18 applies.

Section 18 begins as follows: "For the purpose of preventing the avoiding by individuals ordinarily resident in the United Kingdom of liability to income tax by means of transfers of assets by virtue or in consequence whereof, either alone or in conjunction with associated operations, income becomes payable to persons resident or domiciled out of the United Kingdom, it is hereby enacted as follows: (1) Where such an individual has by means of any such transfer either alone or in conjunction with associated operations, acquired any rights by virtue of which he has, within the meaning of this section, power to enjoy, whether forthwith or in the future, any income of a person resident or domiciled out of the United Kingdom, which, if it were income of that individual received by him in the United Kingdom, would be chargeable in income tax by deduction or otherwise, that income shall, whether it would or would not have been chargeable to income tax apart from the provisions of this section, be deemed to be income of that individual for all the purposes of the Income Tax Acts." The appellant correctly argues that "any such transfer" in sub-section (1) means any "transfer of assets by virtue or in consequence whereof, either alone or in conjunction with associated operations, income becomes payable" to the company. He then contends—and this is the pinch of the case—that trade profits made by a partnership cannot be said to be income a share of which "becomes payable" to one of the partners. One partner, it is said, is not a creditor of the partnership; the share of partnership profits to which the Latjohn Trust Co. became entitled could not, in this view, be described as income which "became payable" to the company.

The answer to this argument is to be found in the powerful judgment of Lawrence, J., and again in a passage from the judgment of the Master of the Rolls which I would respectfully adopt as expressing with the greatest clearness and precision the true view of the application of Section 18 to the facts of this case. Speaking for the Court of Appeal, Lord Greene declared his disagreement with the appellant's arguments and continued: "The share of the profits of the partnership to which the company is entitled is that share which comes to it in accordance with the terms of the partnership. The company is entitled to call upon its partner to do whatever may be necessary, for example, by signing a cheque on the banking account of the partnership, to enable the company to obtain its share. In the partnership accounts the company's undrawn share of profits would appear as a debt owing to the company. If the profits were under the control of the other partner, the company could by appropriate proceedings compel him to

pay over its share. If this is not income 'payable' to the company, we do not know what it is. With regard to the argument that it was not the transfer of assets which produced the income but the activities of the partners, we agree with the argument submitted by the Attorney-General that those activities are 'associated operations' within the definition of that phrase in sub-section (2). By that sub-section, so far as is relevant, an associated operation means, in relation to any transfer, 'an operation of any kind effected by any person in relation to any of the assets transferred', words of the widest import which, in our judgment, clearly cover the operation of turning the assets to account."

These words of the Master of the Rolls completely justify the conclusion that the appellant's attempt to avoid British income tax and surtax by these artificial arrangements has been frustrated by the Act of 1936. This is not a case requiring an examination of previous authority, but I may add that, in my opinion, the two decisions cited by the appellant on the meaning of "annual payment" in Section 105 of the Income Tax Act, 1842 (*Psalms and Hymns (Trustees of) v. Whitwell* and *R. v. Special Income Tax Commissioners; Shaftesbury Homes and Arethusa Training Ship, Ex parte*³) have no bearing here. A recent decision of this House in *City of London Income Tax Commissioners v. Gibbs*³ goes to show that the technical view of the nature of partnership in English law cannot always be taken in applying the law of income-tax.

I move that the appeal be dismissed with costs.

THE LORD CHANCELLOR.—My Lords, I am authorised by my noble and learned friends Lord Atkin and Lord Russell of Killowen to say that they concur in the opinion which I have delivered.

LORD THANKERTON.—I concur.

LORD PORTER.—The conclusion which your Lordships have to reach in this case depends upon the construction and effect of Section 18 of the Finance Act of 1936. That section and the facts upon which its provisions must operate in the circumstances under consideration have already been set out, and it is unnecessary to repeat them. The section contains a proviso exempting cases where the subject shows to the satisfaction of the Special Commissioners that the transfer dealt with was effected for some purpose other than avoiding liability to taxation. This proviso was amended in 1938 so as to have a stricter application, but whether the earlier or later provisions be applicable the Commissioners have found (and it is now conceded that we are bound by their finding) that in the present instance they are not so satisfied.

(1) (1890) 3 Tax Cas. 7.

(2) (1923) 1 K.B. 393,

(3) (1942) A.C. 402; 10 I.T.R. Suppl. 121.

The main argument, however, presented to your Lordships was centred upon the words "payable to." It was said that those words necessitated the existence of a payer and a payee and that income could not become "payable" out of partnership funds to a company which was a member of the partnership. A partner, it was contended, was already the owner, against other things, of his share of the partnership profits and could no more pay himself out of those profits than an individual could pay himself out of the profits of his own business. No doubt it is true to say that an individual cannot pay himself, if pay be used in its strict sense. But no question of an individual's ability to do so arises here. The only question is whether income can be said to be payable to a partner out of the partnership assets. I think it can. "Payable" is not a term of art, and though a partner cannot sue the partnership or the partners individually in order to recover partnership assets, yet, as the Master of the Rolls points out, he has at his disposal means whereby he can ensure that his share reaches his hands. In such circumstances it seems to me that the word "payable" is appropriately used and accurately conveys the process by which the income finds its way into the pocket of the individual. It would, I think, not inaccurately be described as having been paid to him out of the partnership funds.

The appellants, however, sought to support their argument by the suggestion, that, though Cases 1 and 2 of Schedule D have provided appropriate machinery for calculating what the profit of a business is, no such machinery exists in the case of Section 18 of the Act of 1936. They maintained that this omission showed that moneys earned by the personal carrying on of a business abroad, whether alone or in partnership, were not intended to be subject to tax under this section. No doubt this is a matter for consideration, but it is an element only and not a very important one. I can see no reason why a proper estimate cannot be made where the case requires it. As the Lord Chancellor has already observed, the principles laid down in the cases quoted to your Lordships from 3 and 8 Tax Cas. are not applicable here. They deal with different wording, and in those instances no partnership existed. Whatever may be the true view in the circumstances which existed in them, they do not touch the case where money is receivable by a partner out of partnership property.

I agree that the appeal should be dismissed.

Appeal dismissed.

[IN THE COURT OF APPEAL.]

INLAND REVENUE COMMISSIONERS

v.

D. H. WILLIAMS' EXECUTORS.

LORD GREENE, M.R., SCOTT, L.J., MACKINNON, L.J.

Feb. 17, 1948.

'INCOME'—COMPANY INSURED AGAINST LOSS OF DIRECTORS' SERVICES—DEATH OF DIRECTOR—PAYMENT TO COMPANY UNDER POLICY—PAYMENT NOT RECEIVED ON CAPITAL ACCOUNT—TO BE TREATED AS REVENUE AND LIABLE TO INCOME-TAX.

A limited company took out a policy of insurance in the sum of £ 15,000, for the benefit of the company, to cover loss ensuing on the death or injury by accident of a director, whose special qualifications and experience were of value to the company. The director was killed by accident, and the sum assured was paid to the company, which distributed it among the shareholders:—Held, affirming the decision of Macnaghten, J., that the sum of £ 15,000 must be treated as a payment on revenue account, and not as capital, and therefore it was assessable when received by a shareholder to income-tax and to surtax. The director concerned was rendering services which greatly increased the company's revenue, and the sole purpose of insuring was to protect the company against an expected fall in income if his services were no longer available. The expected fall in revenue was reflected in the amount of the policy, but whether that estimate were right or not was immaterial.

Cases referred to:—

Chibbett v. Robinson & Sons (1924) 132 L.T. 26 ; 9 Tax Cas. 48.

Du Cros v. Ryall (1935) 19 Tax Cas. 444.

Mitchell v. Noble, Ltd. (1927) 96 L.J.K.B. 484 ; (1927) 1 K.B. 719 ; 11 Tax Cas. 372.

Murphy v. Gray & Co. (1940) 109 L.J.K.B. 771 ; (1940) 2 K.B. 175 ; 23 Tax Cas. 225 ; 91 T.R. Suppl. 1.

R. v. British Columbia Fir and Lumber Co. (1932) 101 L.J.P.C. 113 ; (1932) A.C. 441.

Appeal from a judgment of Macnaghten, J.

The facts are set out in the judgment of Lord Greene, M.R.

Daynes, K.C., and Scrimgeour, for the Appellants.

The Attorney-General (Sir Donald Somervell, K.C.) and R.P. Hills, for the Respondents.

JUDGMENT.

LORD GREENE, M.R.—It is conceded in this appeal that if the sum in question was not of a nature to attract income-tax in the hands of the company it cannot be taxed in the hands of the shareholder, whose executors are the appellants, either for income-tax or for surtax. The

sole question, therefore, which we have to consider is whether or not this sum was in the hands of the company a receipt on capital account, or a receipt on revenue account. The fact that the company has agreed to have it treated as between itself and the Inland Revenue as a receipt on revenue account cannot bind the present appellants, who are not affected by the view which the company may have taken.

The difficulty lies, as it does so often, in the application of principles to the facts of an individual case; and in this class of case, different minds may well take different views. I have come to the conclusion that the decision of Macnaghten, J., was right. The first thing to do is to examine the nature of the payment which the company received. It was a sum of £ 15,000, received under a policy taken out for the benefit of the company covering injury or death by accident of Mr. Crawford, one of the directors of the company. It was a very small company. There were three principal shareholders and directors, and Mr. Crawford was a gentleman who had very special experience and knowledge of bloodstock, with the sale and purchase of which the company's business was mainly concerned. The nature of his special value to the company is set out in the case stated, and I need not read the passages which refer to it. The company adopted the policy of effecting insurances of a similar character in respect of Mr. Crawford and also in respect of the other two directors, who, in different ways, appear to have had qualifications and experience of special value to the company. But Mr. Crawford obviously stood in a category by himself. The object of the insurance was not to cover any temporary loss. That is stated in the case, although when one comes to look at the policy it is not quite clear how that conclusion was reached by the Special Commissioners. But the suggestion out of which the insurance materialised was that, in the event of Mr. Crawford's death, the company's business would suffer and his family would not get much for his shares. The latter part of that sentence does not seem to alter the real character and object of this insurance, which was quite clearly to give the company some money to make up for the loss which it would suffer if it were deprived of the very valuable services of Mr. Crawford.

It is clear from the case that Mr. Crawford was not bound to the company by any contract. He could have severed his connection with it, or he could have ceased to perform the very useful services which he was performing. But that, to my mind, does not affect the matter. From the business point of view Mr. Crawford's connection with the company was one which obviously was likely to endure, and the absence of any contract of service binding him to the company does not

alter the business position, which was that, so long as he remained there, he would naturally continue to do what he had done in the past and give the company the benefit of his great experience. The case, therefore, may be treated, it seems to me, in exactly the same way as a case in which a valuable servant is bound by a contract, long or short, and the benefit of his services is protected, so to speak, by a policy of insurance taken out by the employer. The policy contained what is called a compensation schedule, and it is, on the face of it, perhaps more appropriate to a policy designed to compensate an individual in respect of injury by accident; but that was not the object of this policy. It was not a policy such as that dealt with in the case of *Murphy v. Gray & Co.*¹ The object of the policy in that case was to put the company in funds in respect of payments to employees which, either through a legal obligation or through a moral obligation, it might be called upon to make. In that respect it differs from the purpose of the present policy, which was not to enable the company to make payments to Mr. Crawford, but to give the company something to make up for the loss which the company would sustain if it were to be deprived of Mr. Crawford's services. Under the policy a sum of £15,000 was payable in the case of death or disabling injuries of a specified character, the occurrence of which would obviously have interfered with his services, or deprived the company of them altogether; then there is a provision of £50 a week in respect of temporary partial disablement from engaging in or giving attention to profession or occupation. Bearing in mind the object of this policy, if Mr. Crawford had, for instance, suffered a temporary disablement over a period of six months, and the company had thereby been deprived of his services during that period, the company would, under this policy, have been receiving £50 a week, and that £50 a week would have been received by it not for the purpose of handing it over to Mr. Crawford but for the purpose of putting it into its own coffers in order to make up in whole or in part for the loss which it would suffer by being deprived of his services during that period. The provisions of the policy therefore fall into line with the general purpose which the company had in taking it out. In point of fact, what happened was that Mr. Crawford unfortunately was killed in an accident. The company therefore was deprived for ever of his services in the future, and its assets were increased by the sum of £15,000 received under the policy. That sum was distributed among the shareholders. What we have to consider is whether that sum of money received in the circumstances which I have stated and being of the nature which I have stated, is to be treated for income-tax purposes as capital or income.

(1) (1940) 23 Tax Cas. 225; 9 I.T.R. Suppl. 1.

It is useful to consider whether there is any broad class into which payments of this character can be said to fall. I think it just to observe as a purely general proposition that in the case of a trading company both goods and services fall into the same class. The expenditure incurred in procuring the goods or producing the goods in which a person trades and the benefits derived from disposing of those goods are obviously of a revenue character. Similarly the expenditure incurred by a person in securing the services of his employees and the benefits derived from those services, reflected as they are in the output and profits of the employer, are again, generally speaking, of a revenue character. The matter can be carried a little further in the case of goods. Not merely are the profits derived from the sale of goods in which a person trades of a revenue character, but insurance moneys received in respect of the loss of trade goods are proper receipts to appear in a revenue account. If a company insures its stock of goods against fire and that stock is destroyed by fire, however great and valuable it may be, the receipts must be treated in exactly the same manner as receipts from a sale of the goods would have been treated. The trader, it is true, as has been said, does not trade in fires but in goods, but if he disposes of the whole of his stock by sale, or if the whole of his stock is destroyed by fire and the insurance money is received, there can be no ground for differentiating for tax purposes between the purchase money and the insurance money.

It seems to me that the benefits derived from a service contract fall into the same broad class. Suppose a company has a particularly valuable servant engaged under a contract of service. So long as that contract remains in force the salary which the company pays is expenditure on revenue account. The benefits which the company receives are reflected in its output and the profits that it makes. They are equally matters for revenue account. If during the course of that employment the servant is temporarily incapacitated, the company's revenue account is affected by reason of the fact that during the incapacity it produces less goods or earns less profits. It may say to itself: "The services of this employee are so important for our business that it is worth our while by way of insurance to protect ourselves against the loss which we shall suffer in our trade if he is temporarily incapacitated." That loss is, of course, of two kinds: (1) the payment of salary during the incapacity, and (2) the actual loss of the profits which the company would otherwise have made. If the company takes out a policy for a sum which the directors estimate will fairly represent the loss or part of the loss—it matters not which—that they will suffer if they are deprived of those services, can it be said that the £ 50 a week

or whatever the figure may be, that the company receives under such a policy is anything but a revenue receipt? It seems to me that the insurance moneys received to cover the company against the revenue loss which it suffers by being deprived of those services are receipts on revenue account and nothing else. But supposing the company carries the matter a step further and says: "We shall suffer loss not merely by the temporary incapacity of our servant, but if he dies during the period of service we shall suffer a very much greater loss", and, with that in mind, it decides to extend the insurance to cover the death of this valuable servant and insures his life accordingly for a lump sum. Whether or not the directors' estimate of the loss which they will suffer by the death of that servant is accurately reflected in the sum which they fix for his insurance is neither here nor there. The important matter is the object of the insurance, which may or may not be entirely achieved according to the accuracy of the estimate made. What would be the position if after taking out that policy the employee happened to die, with the result that the company was deprived of those benefits on revenue account which it would have received if it had continued to enjoy his services?

There is no magic here in the distinction between a lump sum and a periodical sum. The question is: What is the nature of the sum?—and although the fact there is a lump sum paid once and for all rather tends to colour the question and to make one inclined to regard it as of a capital nature, that, in my opinion, is apt to be misleading. To go back to the example I took a moment ago of temporary incapacity, I myself cannot see what difference there can be between a case where the insurance takes the form of a weekly payment and a case where it takes the form of a lump-sum payment to cover some defined period. Similarly in the case of death, the fact that a lump sum is paid cannot, in my view, differentiate the case from one where a periodical payment is made year by year under a policy during the unexpired part of the contract of service. Suppose that the policy, instead of providing that the company should receive a lump sum on death, provided that during the remainder of the period of service between the death and the end of the term the company should receive a yearly sum, the object being to compensate it for the estimated loss it would sustain, I cannot see that there can be any difference between the two cases. My view that insurance moneys received in circumstances such as those which I have described are really receipts on revenue account can be tested in the case, for instance, of a particularly valuable commission agent. A company might be in a position to estimate with very considerable accuracy the amount of business which it was likely to get

from a particular commission agent, and it might be in a position to fix very closely the appropriate sum for insurance against his incapacity or death. It seems to me that whether the amount of the insurance is fixed on an estimate which in the circumstances can be made with substantial accuracy or whether it is fixed on the basis of a broad estimate by the employer, as to the sum for which it will be worth his while to insure the employee makes no difference. Therefore, it seems to me that in this case the receipt must be treated as a receipt on revenue account.

The matter can be looked at from rather a different point of view. I do not wish to lay down any general proposition which would lead to the result that the test in the case of payments is necessarily the same as the test in the case of receipts. In the case of payments the question whether they are to be treated as deductible expenses is complicated by the special provisions of the Income Tax Acts which lay down certain categories of expenditure which are not deductible. But looking at the matter from the broader point of view, on the question whether a particular item of expenditure or a particular item of receipt falls into the category of revenue expenditure or a receipt, or capital expenditure or receipt, I think assistance is to be obtained from examination of cases which have dealt with the question of expenditure. I do not propose to go into the various cases which have been cited to us, but the case of *Mitchell v. Noble Ltd.*¹ is perhaps the best example. That was a case, putting it shortly, in which the company found it advisable to pay money in order to get rid of a servant whose services they no longer required and who in point of fact was embarrassing to the company. It was held that the sums paid in order to get rid of that servant were admissible deductions. When an employer or a company finds it desirable to expend money in getting rid of an onerous contract of service, the expenses incurred are revenue expenses, but it does not seem to me to follow that the money received in respect of the loss of a beneficial contract of service falls into the same category; and, apart from the fact that no actual contract existed, that appears to me to be the present case. There is one more case to which I may refer, the case in the Privy Council to which our attention was called: *R. v. British Columbia Fir and Lumber Co.*² It is true that the Income Tax Act which was being dealt with there was different in language from our own Income Tax Acts, but it does afford an illustration of what happens in the matter of insurances of a particular character. I think the result of that case is of general application in

(1) (1927) 11 Tax Cas. 372.

(2) (1932) A.C. 441.

this sense : the particular matter of insurance that was being dealt with there was an insurance against loss of profits. A manufacturer can, of course, insure his factory against fire. The receipts from that insurance will obviously be capital receipts. But supposing he goes further, as the manufacturer did in that case, and insures himself against the loss of profits which he will suffer while his factory is out of action, it seems to me it is beyond question that sums received in respect of that insurance against loss of profits must be of a revenue nature. Similarly the moneys received under a policy of insurance against the loss of profits through the loss of a valuable servant must in essence be receipts of a revenue nature. As I have already said, I can draw no distinction between the case where the receipts under such an insurance take the form of periodical payments and the case where they take the form of a lump sum paid down.

The cases which were relied upon by counsel for the appellants do not, in my opinion, support his proposition. The two main ones were *Chibbett v. Robison & Sons*¹ and *Du Cros v. Ryall*². The former was a case in which a firm of ship managers, whose sole business consisted in managing the ships of a particular company, received in the liquidation of that company a sum of £50,000. The question was whether that sum ought to be treated as part of the profits of their business. When the employing company went into liquidation the business of the firm of ship managers came to an end, and the receipt was held to be not a receipt from business activities, but in the nature of a voluntary payment, made as compensation for the loss of the profits of their employment under the company which had terminated. It seems to me that that stands in quite a different category from the present case. The other case, *Du Cros v. Ryall*³, was a case in which the general manager of a company working on a fixed salary and a commission on profits had a contract for a fixed term which was repudiated by the employing company. He brought an action which was compromised, and the question was whether the large sum paid as agreed damages under that compromise was assessable under Schedule E. The contract of service was at an end. The source of income had disappeared, and the sum paid by way of damages could not be regarded as a sum derived from the employment. It was something which arose outside the employment. It was something to which Mr. Du Cros became entitled by reason of the disappearance of the employment. It was therefore again of quite a different character from insurance moneys received by a going concern in order to recoup it for the loss suffered through the death or disablement of a valuable servant, or, as in this case, of a person associated with the company without a contract of service whose services, from a business point of view, the company might reasonably anticipate would continue.

In my opinion, as I have said, the learned Judge came to the right conclusion in this case, and the appeal must be dismissed with costs.

SCOTT, L.J.—I agree.

MACKINNON, L.J.—I agree.

Appeal dismissed.

Leave to appeal to the House of Lords.

(1) (1924) 9 Tax Cas. 43.

(2) 1935) 19 Tax Cas. 444.

Income Tax Reports.

VOLUME XI—1943.

(STATUTES).

INCOME-TAX PROCEEDINGS VALIDITY ORDINANCE, 1943.*

ORDINANCE No. IV OF 1943.

AN ORDINANCE

to establish the validity of certain appointments as Income-tax Officers of, and certain proceedings under the Indian Income-tax Act, 1922, taken by, persons designated as Assistant Income-tax Officers.

WHEREAS an emergency has arisen which makes it necessary to establish the validity of certain appointments as Income-tax Officer of and certain proceedings under the Indian Income-tax Act, 1922, taken by, persons designated as Assistant Income-tax Officers :

Now, THEREFORE, in exercise of the powers conferred by Section 72 of the Government of India Act, as set out in the Ninth Schedule to the Government of India Act, 1935, the Governor-General is pleased to make and promulgate the following Ordinance :—

Short title and commencement.

1. (1) This Ordinance may be called the Income-tax Proceedings Validity Ordinance, 1943.

(2) It shall come into force at once.

Validity of appointment as Income-tax Officer of Assistant Income-tax Officer and of proceedings taken by them.

2. Where, whether before or after the commencement of this Ordinance, any person designated as an Assistant Income-tax Officer has been appointed to be or to discharge the functions of an Income-tax Officer for any of the purposes of the Indian Income-tax Act, 1922, and where, whether before or after the commencement of this Ordinance, a person designated as an Assistant Income-tax Officer, appointed to be or to discharge the functions of an Income-tax Officer, has given or served any notice or taken any action whatsoever under the said Act for the purpose of or in connection with the making of an assessment under the said Act, such person shall be deemed to be and always to have been validly appointed as an Income-tax Officer for the purposes of the said Act, and no

* This Ordinance which was published in the Gazette of India extraordinary dated January 16, 1943, seeks to remove the difficulty caused in the administration of Income-tax law by the recent decision of the Bombay High Court in *Govindram Seksaria, In re*, reported *infra* at p. 104.—Ed.

act purporting to have been done by such person as an Income-tax Officer, and no notice purporting to have been given or served by such person as an Income-tax Officer shall be called in question merely on the ground of any irregularity or defect in the manner of his appointment as an Income-tax Officer.

INCOME-TAX REFERENCES AND APPLICATIONS---MADRAS HIGH COURT RULES.*

The following rules shall regulate the procedure to be adopted in regard to references and applications to the High Court under Section 66 of the Act, as amended by Part II of the Indian Income-tax (Amendment) Act, 1939, read with the Government of India Notification No. 2, Finance (Central Revenues) Income-tax, dated 18th January 1941 :—

1. References under Section 66 (1) of the Act by the Appellate Tribunal stating a case for the opinion of the High Court shall, on receipt thereof by the Registrar, be numbered as Referred Cases but no Court fee shall be levied on such references by the Registrar.

2. The Registrar, Appellate Tribunal, shall together with the letter of reference submit two copies of the said letter and of any records necessary for the consideration of the reference.

3. (a) On the said reference being numbered as a Referred Case, the Registrar shall fix a day for the hearing of the case and intimation thereof shall be given to the Appellate Tribunal and to the Commissioner of Income-tax.

(b) Within a fortnight of the receipt of the intimation referred to in sub-clause (a) above the Commissioner of Income-tax shall file a memorandum giving particulars for service on the parties concerned in Form I of Appendix IV of Appellate Side Rules with Court-fee labels attached for the fees prescribed for service of notice on them.

4. (a) Any application under Section 66 (2) of the Act requiring the Appellate Tribunal to state a case for the opinion of the High Court shall be by a Civil Miscellaneous Petition. The petition shall be verified and shall contain in precise language a statement of the point of law upon which the case is to be stated and shall set out concisely the material facts and the proceedings which have taken place before the Income-tax Officers and the Appellate Tribunal. Copies of the orders of the Income-tax Officer, of the Appellate Assistant Commissioner of Income-tax and of the Appellate Tribunal under Section 38 (4) of the Act out of which the question of law arose and under Section 66 of the Act refusing to state a case shall be filed with the petition.

* Published in the Fort St. George Gazette supplement dated March 31, 1942.

(b) An Application under Section 66 (3) of the Act shall also be by a Civil Miscellaneous Petition which shall be verified and which shall set out concisely the proceedings which have taken place before the Appellate Tribunal. It shall be accompanied by two copies of the orders of the Appellate Tribunal disposing of the case.

5. With the petition shall be filed two spare copies thereof and of the orders referred to in rule (4) supra. The two spare copies of the petition and orders shall be neatly typed on substantial white paper, paged, indexed and stitched in book form. The petition shall also be accompanied by a memorandum giving particulars for service on the respondent in Form No. I of Appendix IV, Appellate Side Rules with court-fee labels attached for the fees prescribed for service of notice on him.

6. (a) As soon as the Registrar fixes a day for the hearing of the Referred Case or Petition, a notice of the date of hearing in the form herewith annexed shall be issued to the parties concerned.

(b) The rules in Chapter VII of the Appellate Side Rules shall, as far as may be applicable, apply to the service of notices in Referred Cases and Petitions under Section 66 of the Act.

7. References under Section 66 (1) and Applications under Section 66 (2) or (3) of the Act shall be posted as soon as service of notice has been effected before such Bench of two Judges as the Chief Justice may from time to time appoint.

8. All cases referred or stated by the Appellate Tribunal shall, as far as possible, be divided into paragraphs, numbered consecutively and shall concisely state such facts and refer to such documents, with copies of the latter annexed, as may be necessary to enable the Court to decide the question raised thereby.

9. The Appellate Tribunal shall settle the case in its final form, forward the case as thus settled to the High Court and supply three copies thereof to the Commissioner of Income-tax and the Assessee, intimating to them at the same time, the date on which the case stated by the Tribunal was sent to the High Court.

10. Upon the argument of such Reference or Petition, the Court and the parties shall be at liberty to refer to the whole of the contents of the documents annexed to the case.

11. The statement of the case shall set out in the concluding paragraph thereof the point of law to be decided as stated in the application of the assessee or of the Commissioner of Income-tax or any modified form thereof which the High Court may have ordered.

12. The Court disposing of the case shall fix the fees payable by or to either party in its absolute discretion.

ANNEXURE.

*Form of notice under rule 6.*IN THE HIGH COURT OF JUDICATURE AT MADRAS.
Appellate Side.

| | | |
|--------------------------|---------------------------------------|-------------|
| <u>Referred Case No.</u> | <u>of 19 .</u> | |
| C. M. P. No. | of 19 . | |
| ... | Applicant in | on the file |
| | <u>of the Appellate Tribunal</u> | |
| | Petitioner. | |
| | <i>versus</i> | |
| ... | Respondent in | on the |
| | <u>file of the Appellate Tribunal</u> | |
| | Respondent. | |

Take notice that a case has been stated and referred by the *Appellate Tribunal* for the opinion of the Honourable Judges of the High Court under the date the day of 19
or that a petition has been made to the High Court on the
 day of 19

by the above-named petitioner to require the *Appellate Tribunal* to state a case and refer it to the High Court for the opinion of the Honourable the Judges or to require the Appellate Tribunal to treat the application made by him to the Appellate Tribunal under Section 66 (1) of the Act as made within the prescribed time. You are hereby required to appear before the said High Court on the
 day of 19 in person or by a duly

authorized pleader and be prepared to argue the said reference or petition and that, in default of your appearance, the said reference or petition may be heard or determined in your absence.

By virtue of the powers conferred by the Government of India Act 1935 (26 Geo., 5 Ch. 2), the Letters Patent of the High Court of Judicature at Madras as amended from time to time and of all other powers hereunto enabling, the High Court has made the following amendments to the rules of the High Court, Original Side, 1927. They shall come into force on the date of publication in the *Fort St. George Gazette*.*

(1) In Order XLVII, the following shall be substituted for the preamble to the Order, namely:—

The following rules shall regulate the procedure to be adopted in regard to References and Applications made to the High Court under Section 66 of the Act before its amendment by Part II of the Indian Income-tax (Amendment) Act, 1939, read with the Government of India Notification No. 2, Finance (Central Revenues) Income-tax, dated 18th January 1941.

(2) In Order XLVII, in rule 8, for the words "Such Bench of three Judges," the words "Such Bench of two Judges" shall be substituted.

* Published in the Fort St. George Gazette supplement dated March 31, 1942.

Income Tax Reports.

VOLUME XI—1943.

(STATUTES.—*Contd.*)

THE INDIAN FINANCE ACT, 1943.

(Act VIII of 1943).

[Received the assent of the Governor-General on the
29th March, 1943.]

An Act, to fix the duty on salt manufactured in, or imported by land into, certain parts of British India, to fix maximum rates of postage under the Indian Post Office Act, 1898, to continue for a further period of one year the additional duties of customs imposed by Section 6 of the Indian Finance Act, 1942, to fix rates of Income-tax and super-tax, to continue the charge and levy of excess profits tax and fix the rate at which excess profits tax shall be charged, and to amend the Indian Finance (Supplementary and Extending) Act, 1931.

Whereas it is expedient to fix the duty on salt manufactured in, or imported by land into, certain parts of British India, to fix maximum rates of postage under the Indian Post Office Act, 1898 (VI of 1898), to continue for a further period of one year the additional duties of customs imposed by Section 6 of the Indian Finance Act, 1942 (XII of 1942), to fix rates of income-tax and super-tax, to continue the charge and levy of excess profits tax and fix the rate at which excess profits tax shall be charged, and to amend the Indian Finance (Supplementary and Extending) Act, 1931;

It is hereby enacted as follows:

Short title and extent. 1. (1) This Act may be called the Indian Finance Act, 1943.

(2) It extends to the whole of British India.

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Income-tax and super-tax. 5. (1) Subject to the provisions of sub-sections (2) and (3),—

(a) income-tax for the year beginning on the 1st day of April, 1943, shall be charged at the rates specified in Part I of Schedule II increased in the cases to which sub-paragraph (b) of paragraph A and paragraph B of that Part apply by a surcharge for the purposes of the Central Government at the rate specified therein in respect of each such rate of income-tax, and

(b) rates of super-tax for the year beginning on the 1st day of April, 1943, shall, for the purposes of Section 55 of the Indian Income-tax Act, 1922, be those specified in Part II of Schedule II

increased in the cases to which paragraphs A, B and C of that part, apply by a surcharge for the purposes of the Central Government at the rate specified therein in respect of each such rate of super-tax.

(2) In making any assessment for the year ending on the 31st day of March, 1944,—

(a) Where the total income of an assessee, not being a company, includes any income chargeable under the head "Salaries" or under the head "Interest on Securities" or any income from dividends in respect of which he is deemed under Section 49B of the Indian Income-tax Act, 1922, to have paid income-tax imposed in British India, the Income-tax payable by the assessee on that part of his total income which consists of such inclusions shall be an amount bearing to the total amount of income-tax payable according to the rates applicable under the operation of the Indian Finance Act, 1942, on his total income the same proportion as the amount of such inclusions bears to his total income;

(b) where the total income of an assessee, not being a company, includes any income chargeable under the head "Salaries" on which super-tax has been or might have been deducted under the provisions of sub-section (2) of Section 18 of the Indian Income-tax Act, 1922, the super-tax payable by the assessee on that portion of his total income which consists of such inclusions shall be an amount bearing to the total amount of super-tax payable according to the rates applicable under the operation of the Indian Finance Act, 1942, on his total income the same proportion as the amount of such inclusions bears to his total income.

(3) In case to which Section 17 of the Indian Income-tax Act, 1922, applies, the tax chargeable shall be determined as provided in that section but with reference to the rates imposed by sub-section (1) of this section, and in accordance with the provisions of sub-section (2) of this section where applicable.

(4) For the purposes of this section and of the rates of tax imposed thereby, the expression "total income" means total income as determined for the purposes of income-tax or super-tax, as the case may be, in accordance with the provisions of the Indian Income-tax Act, 1922.

(5) Notwithstanding anything contained in sub-section (1) or sub-section (2) no tax shall be payable in cases to which sub-paragraph (a) of paragraph A of Part I of Schedule II applies where the assessee deposits with the Central Government in such manner and in accordance with such conditions as the Central Government may by rule prescribe for the purposes of this sub-section an amount representing ;

not less than one rupee for every complete unit of twenty-five rupees by which his total income exceeds seven hundred and fifty rupees.

(6) A deposit made in accordance with the provisions of sub-section (5) shall not in any way be capable of being charged and shall not be liable to attachment under any decree or order of any Civil, Revenue or Criminal Court in respect of any debt or liability incurred by the depositor and neither the Official Assignee nor any receiver appointed under the Provincial Insolvency Act, 1920, shall be entitled to or have any claim on any such deposit.

(7) Where the total income of an assessee referred to in sub-paragraph (b) of paragraph A of Part I of Schedule II does not exceed six thousand rupees, an amount representing one rupee for every complete unit of two hundred rupees of his total income as reduced by the income, if any, exempt from tax under any provision of the Indian Income-tax Act, 1922, or any notification issued thereunder shall be funded for the assessee's benefit and shall be paid to him on such date, not more than twelve months after the termination of the present hostilities, as the Central Government may fix :

Explanation.—In computing the amount to be funded under this sub-section if there is an incomplete unit amounting to one hundred rupees or more it shall be reckoned as a complete unit of two hundred rupees.

(8) Notwithstanding anything contained in sub-section (7) of Section 8 of the Indian Finance Act, 1942, the amount to be funded under that sub-section for the assessee's benefit in respect of any assessment for the year ending on the 31st day of March, 1943, shall be calculated on his total income as reduced by the income, if any, exempt from tax under any provision of the Indian Income-tax Act, 1922, or any notification issued thereunder.

(9) The Central Government may, by notification in the official Gazette, make rules prescribing the manner and conditions referred to in sub-section (5).

6. (1) In sub clause (a) of clause (6) of Section (2) of the Excess Profits Tax Act, 1940, for the words and figures " 31st day of March, 1943 " the words and figures " 31st day of March, 1944 " shall be substituted.

(2) The excess profits tax imposed by Section 4 of the Excess Profits Tax Act, 1940, shall, in respect of any chargeable accounting period beginning after the 31st day of March, 1943, be an amount equal to sixty-six and two-thirds per cent. of the amount by which the profits of the business during that chargeable accounting period exceed the standard profits.

Continuance of
and rate of excess
profits tax.

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SCHEDULE II.

(See Section 5).

PART I.

Rates of Income-tax.

A.—In the case of every individual, Hindu undivided family, unregistered firm and other association of persons not being a case to which paragraph B of this Part applies:—

(a) Where the total income does not exceed Rs. 2,000—

| | Rate. |
|------------------------------------------------------------------------------------------|------------------------|
| 1. On the first Rs. 750 of total income | Nil. |
| 2. On the next Rs. 1,250 of total income | Six pies in the rupee. |
| Provided that no tax shall be payable on a total income which does not exceed Rs. 1,500. | |

(b) Where the total income exceeds Rs. 2,000—

| | Rate. | Surcharge. |
|-------------------------------------------|---------------------------------------|---------------------------------------|
| 1. On the first Rs. 1,500 of total income | Nil. | Nil. |
| 2. On the next Rs. 3,500 of total income | Nine pies in the rupee | Six pies in the rupee. |
| 3. On the next Rs. 5,000 of total income | One anna and three pies in the rupee. | Ten pies in the rupee. |
| 4. On the next Rs. 5,000 of total income | Two annas in the rupee. | One anna and four pies in the rupee. |
| 5. On the balance of total income | Two annas and six pies in the rupee. | One anna and eight pies in the rupee. |

B.—In the case of every company and local authority, and in every case in which under the provisions of the Indian Income-tax Act, 1922, income-tax is to be charged at the maximum rate—

| | Rate | Surcharge. |
|------------------------------|--------------------------------------|---------------------------------------|
| On the whole of total income | Two annas and six pies in the rupee. | One anna and eight pies in the rupee. |

PART II.

Rates of Super-tax.

A.—In the case of every individual, Hindu undivided family, unregistered firm and other association of persons, not being a case to which paragraphs B and C of this Part apply—

| | Rate. | Surcharge. |
|----------------------------------------------|---------------------------|----------------------------------------|
| 1. On the first Rs. 25,000 of total income. | Nil. | Nil. |
| 2. On the next Rs. 10,000 of total income. | One anna in the rupee. | One anna in the rupee. |
| 3. On the next Rs. 20,000 of total income. | Two annas in the rupee. | One anna and six pies in the rupee. |
| 4. On the next Rs. 70,000 of total income. | Three annas in the rupee. | Two annas in the rupee. |
| 5. On the next Rs. 75,000 of total income. | Four annas in the rupee. | Two annas and six pies in the rupee. |
| 6. On the next Rs. 1,50,000 of total income. | Five annas in the rupee. | Three annas in the rupee. |
| 7. On the next Rs. 1,50,000 of total income. | Six annas in the rupee. | Three annas in the rupee. |
| 8. On the balance of total income. | Seven annas in the rupee. | Three annas and six pies in the rupee. |

B.—In the case of every local authority—

| | Rate. | Surcharge. |
|-------------------------------|------------------------|------------------------|
| On the whole of total income. | One anna in the rupee. | One anna in the rupee. |

C.—In the case of an association of persons being a co-operative society, other than the Sanikatta Saltowners' Society in the Bombay Presidency, for the time being registered under the Co-operative Societies Act, 1912, or under an Act of the Provincial Legislature governing the registration of Co-operative Societies—

| | Rate. | Surcharge. |
|---------------------------------------------|------------------------|------------------------|
| 1. On the first Rs. 25,000 of total income. | Nil. | Nil. |
| 2. On the balance of total income. | One anna in the rupee. | One anna in the rupee. |

D.—In the case of every company—

| | Rate. |
|------------------------------|-------------------------|
| On the whole of total income | Two annas in the rupee. |

STATEMENT OF OBJECTS AND REASONS.

The object of this Bill is to continue for a further period of one year the existing rate of salt duty; to increase the postage rate on letters exceeding one tola; to continue the additional duties imposed by Section 6 of Act XII of 1942 and to increase the corporation tax and the Central surcharge on income-tax and super-tax.

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5. *Clause 5* provides for the continuance for a further period of one year of the existing basic rates of income-tax and super-tax and for certain graded increases in the surcharges on income-tax and super-tax.

6. *Clause 6* provides for the continuance of the excess profits tax at the rate of 66½ per cent.

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INDIAN FINANCE (INCOME-TAX) RULES, 1943.

Notification No. 48(24)—I.T./42 dated 3rd April, 1943.

In exercise of the powers conferred by sub-section (9) of Section 5 of the Indian Finance Act, 1943 (VIII of 1943), the Central Government is pleased to make the following rules for prescribing the manner and conditions referred to in sub-section (5) of Section 5 of the said Act, namely :—

1. These Rules may be called the Indian Finance (Income-tax) Rules, 1943.

2. The Indian Finance (Income-tax) Rules, 1942, prescribed for the purposes of sub-section (5) of Section 8 of the Indian Finance Act, 1942, shall apply for the purposes of sub-section (5) of Section 5 of the

Indian Finance Act, 1948, subject to the following modifications and additions, namely :—

In the said Rules—

(a) for the words, brackets and figures “ sub-section (5) of Section 8 of the Indian Finance Act, 1942 ” wherever they occur the words, brackets and figures “ sub-section (5) of Section 5 of the Indian Finance Act, 1948 ” shall be substituted.

(b) for the second proviso to rule 3 the following proviso shall be substituted, namely—

“ Provided further that in the case of a person whose total income includes any income chargeable under the head ‘ salaries ’ or under the head ‘ interest on securities ’ from which tax has been deducted under Section 18 of the Indian Income-tax Act, 1922 (XI of 1922), or dividends in respect of which he is deemed under Section 49 B of the said Act to have paid income-tax himself in British India, the amount of the tax deducted or paid at source may, if he elects to discharge his liability to tax by making a deposit, be transferred wholly or in part, as the case may be, to his income-tax, Defence Savings Bank account and credited to the deposit referred to in the foregoing provisions of this rule. If the amount of tax deducted at source is less than the minimum deposit required to be made in respect of his total income the deficiency shall be made good by him by making a deposit in the manner required by this rule. If the amount of tax is in excess of the minimum deposit the excess shall on his application be refunded to him.”

(c) in rule 3 after the new second proviso the following further proviso shall be inserted, namely :—

“ Provided further that a person, whose total income of the previous year includes any income chargeable under the head ‘ salaries ’ in respect of which the option of having the appropriate portion of the deposit deducted from his salary was exercised by him under any rule for the time being in force, may make a further deposit, if necessary, to cover the liability, if any, in respect of his total income including salary.”

(d) in rule 6 the words “ and is not a person from whose salary a deposit has been deducted under rule 8 ” shall be omitted.

(e) in Form A annexed to the said Rules for the figures “ 1942 ” the figures “ 1948 ” shall be substituted and the following shall be added to paragraph 2 thereof—

“ In respect of the income from salaries/interest on securities/Dividends shown in paragraph 1 a sum of Rs. _____ has been deducted or is deemed to have been paid at source and therefore the balance of Rs. _____ only no amount has been deposited in the Defence Savings Bank account.”

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“Annual charge not being capital charge”—*See* Income-tax Act (XI of 1922), Sec. 9 (1) (iv).

“Assessee”, Meaning of—*See* Income-tax Act (XI of 1922), Sec. 10 (2) (vi).

“Income”—*See* Income-tax Act (XI of 1922), Sec. 3.

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“Original cost to assessee”—*See* Income-tax Act (XI of 1922), Sec. 10 (2) (vi).

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